AUTHORIZATIONS—MARAD AND FMC

HEARING

BEFORE THE

SUBCOMMITTEE ON MERCHANT MARINE

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

SECOND SESSION

ON

S. 2336

TO AUTHORIZE APPROPRIATIONS FOR FISCAL YEAR 1983 FOR CERTAIN MARITIME PROGRAMS OF THE DEPARTMENT OF TRANSPORTATION, AND FOR OTHER PURPOSES

APRIL 20, 1982

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AUTHORIZATIONS—MARAD AND FMC

TUESDAY, APRIL 20, 1982

U.S. Senate,
Committee on Commerce, Science, and Transportation,
Subcommittee on Merchant Marine,
Washington, D.C.

The subcommittee convened, pursuant to notice, at 10:05 a.m., in room 235, Russell Senate Office Building, Hon. Slade Gorton (chairman of the subcommittee) presiding.

Staff members assigned to this hearing: Terry Spilsbury, staff counsel and John D. Hardy, minority staff counsel.

OPENING STATEMENT BY SENATOR GORTON

Senator Gorton. We will call this meeting to order.

This hearing is convened to consider S. 2336, a bill which I introduced with Senators Packwood, Stevens, and Kasten, to authorize appropriations for maritime programs executed by the Maritime Administration and the Federal Maritime Commission at levels requested by the President for fiscal year 1983.

We will begin the hearing with the hope that one or more Senators will join us during its course. There is a Democratic caucus going on. Senator Inouye does hope to be here before the meeting is over. In any event, he and Senator Long have asked to reserve the right to submit questions in writing, which request is of course granted.

Like most other Federal programs, those aimed at the maritime industry are under the pressures of budgetary constraints. The funding levels sought by the administration and authorized by this bill represent essentially a decision to place these programs on hold pending completion of the administration's maritime policy review.

Nevertheless, in reaction to these budgetary pressures, it has been necessary to make several significant policy changes in S. 2336.

First, as was the case last year, no funds are authorized for construction differential subsidies. This bill extends and makes permanent the authority of U.S.-flag subsidized vessel operators to engage foreign shipyards to construct, reconstruct, and repair their vessels. The use of tax deferred capital construction funds for foreign construction, however, is specifically precluded.

Second, the administration has asked Congress to set annual limits on new commitments in title XI vessel construction loan guarantees. This bill includes such a limit set at the same level as set by the administration in 1982, $675 million, or about 10 percent more than the administration's recommendation for fiscal year

1983. It makes clear, however, that annual limits are to be set, if at all, only in authorization acts such as the one before us now.

S. 2336 would also make technical amendments to title XI of the Merchant Marine Act of 1936 in order to provide greater flexibility to the Secretary of Transportation to foreclose on a vessel upon default of a guaranteed loan without extinguishing the financing agreement.

Additionally, this bill would amend the Bankruptcy Reform Act of 1978 to restore a provision, omitted inadvertently in the 1978 revision, to permit the Secretary of Transportation to foreclose on title XI mortgages before the vessel operator's assets are frozen.

It disturbs me that we must again seek ad hoc alterations in our programs. This period of adjustment is not unique to maritime policy, though, and I have great confidence that the administration will be able to come up with a constructive, comprehensive, promotional policy in the coming months. Admiral Shear deserves tremendous credit for his constant effort to formulate that kind of policy.

In the meantime, I wish to assure the maritime industry of my resolve to work with the administration to implement an effective strategy consistent with fundamental tenets of sound Federal fiscal and regulatory policy.

We are nearing completion of our intensive focus on regulatory policy over the liner industry, and I am confident that we will enact S. 1593 this year. Many people, both inside and outside of the maritime industry, who have provided constructive assistance have helped make S. 1593 a good and responsible bill. This is true especially of Chairman Green for responsively marshaling the expertise of the Federal Maritime Commission in our aid.

I also expect to hold hearings on Government-preference cargo in May with an eye to instilling a cooperative attitude among those departments which ship substantial Government cargo. And, I guarantee that when an administration policy is announced this subcommittee will act promptly to consider it.

Only one further comment before we proceed. We are focusing today on Federal programs and their funding. It is a mistake, however, to take the view that the problems of the maritime industry are primarily problems connected with Government policies. For our efforts in fashioning revised policies to work successfully, it is absolutely necessary that every facet of the maritime industry adjust, innovate, and, in some cases, even sacrifice.

[The bill follows:]

97TH CONGRESS
2D SESSION

S. 2336

To authorize appropriations for fiscal year 1983 for certain maritime programs of the Department of Transportation, and for other purposes.

IN THE SENATE OF THE UNITED STATES

APRIL 1 (legislative day, FEBRUARY 22), 1982

Mr. GORTON (for himself, Mr. PACKWOOD, Mr. STEVENS, and Mr. KASTEN) introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

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A BILL

To authorize appropriations for fiscal year 1983 for certain maritime programs of the Department of Transportation, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That funds are authorized to be appropriated for certain maritime programs of the Department of Transportation for the fiscal year 1983, as follows:

(1) for payment of obligations incurred for operating differential subsidy, not to exceed $454,010,000;

(2) for expenses necessary for research and development activities, not to exceed $16,800,000;

(3) for expenses necessary for operations and training activities, not to exceed $71,013,000, including not to exceed—

(a) $6,516,000 for reserve fleet expenses;

(b) $29,607,000 for maritime education and training expenses, including not to exceed $17,251,000 for maritime training at the Merchant Marine Academy maintained under section 1303 of the Merchant Marine Act, 1936, as amended, $10,668,000 for financial assistance to State maritime academies assisted under section 1304 of the Act, and $1,688,000 for expenses necessary for additional training provided under section 1305 of the Act; and

(c) $34,890,000 for other operations and training expenses.

Sec. 2. Section 615 of the Merchant Marine Act, 1936 (46 U.S.C. 1185), is amended to read as follows:

"Sec. 615. Notwithstanding any other provision of this Act, an operator receiving or applying for operating differential subsidy under this title may construct, reconstruct, or acquire its vessels of over five thousand deadweight tons in a foreign shipyard. Vessels constructed, reconstructed, or modified pursuant to this section shall be deemed to have been United States built for the purposes of this title, section

901(b) of this Act, and section 5(7) of the Port and Tanker Safety Act of 1978 (46 U.S.C. 391(a)(7)): *Provided,* That the provisions of section 607 of this Act shall not apply to vessels constructed, reconstructed, modified, or acquired pursuant to this section.".

SEC. 3. Section 1103(f) of the Merchant Marine Act, 1936 (46 U.S.C. 1273(f)), is amended by adding at the end thereof the following new sentence: "No additional limitations may be imposed on new commitments to guarantee loans for any fiscal year, except in such amounts as established in advance in annual authorization acts."

SEC. 4. The Secretary of Transportation shall not enter into new commitments to guarantee loans under section 1103(f) of the Merchant Marine Act, 1936 (46 U.S.C. 1273(f)) in an amount greater than $675,000,000 during fiscal year 1983.

SEC. 5. (a) Section 1104(a)(3) of the Merchant Marine Act, 1936, as amended (46 U.S.C. 1274(a)(3)), is amended by inserting after the word "Fund" the words ", or for which related obligations were accelerated and paid by the Secretary of Transportation,".

(b) Section 1104(h) of such Act (46 U.S.C. 1274(h)) is amended by inserting after the word "acceleration" the word ", assumption,".

(c) The first sentence of section 1104(a) of such Act (46 U.S.C. 1275(a)) is amended by inserting after the word "demand" the following: "(unless the Secretary of Transportation shall, in his sole discretion, have assumed and performed the obligor's rights and duties relating to such payment of principal and interest and any applicable fiduciary fees),".

(d) Section 1105(b) of such Act (46 U.S.C. 1275(b)) is amended to read as follows:

"(b) In the event of a default under a mortgage, loan agreement, or other security agreement between the obligor and the Secretary of Transportation, the Secretary of Transportation may, at his option and sole discretion—

(1) notify the obligee or his agent of such default and the assumption by the Secretary of Transportation of the obligor's rights and duties relating to the payment of principal and interest under an obligation guaranteed under this title and any applicable fiduciary fees; or

(2) notify the obligee or his agent of such default and the obligee or his agent shall have the right to demand at or before the expiration of such period as may be specified in the guarantee or related agreements, but not later than sixty days of such notice, payment by the Secretary of Transportation of the

unpaid principal amount of said obligation and the unpaid interest thereon. Within such period as may be specified in the guarantee or related agreements, but not later than thirty days from the date of such demand, the Secretary of Transportation shall promptly pay to the obligee or his agent the unpaid principal amount of said obligation and unpaid interest thereon to the date of payment.".

(e) The first sentence of section 1105(c) of such Act (46 U.S.C. 1275(c)) is amended by inserting after the word "payment" the words "or assumption" and by inserting after "Secretary of Transportation", the first time it appears, the words ", in his sole discretion,".

Sec. 6. Section 362(b) of title XI, United States Code, is amended by inserting "(i)" before "Secretary of Housing and Urban Development" and by adding at the end thereof the following:

"(ii) The Secretary of Transportation to foreclose a mortgage on a vessel or vessels pursuant to the Ship Mortgage Act, 1920, as amended, held by said Secretary under the provisions of sections 1101–1110 or section 207 of the Merchant Marine Act, 1936, as amended; or".

Sec. 7. Commencing with fiscal year 1983, appropriation of funds to carry out the laws administered by the

Federal Maritime Commission shall be subject to annual authorization.

SEC. 8. Funds are authorized to be appropriated in the amount of $10,378,000 for the use of the Federal Maritime Commission for the fiscal year 1983.

Senator GORTON. We have many witnesses to hear from this morning, so I encourage each of them to be as brief as possible in his oral statement. We have reviewed each of your written statements, and they will be included in full in the record. Additional comments to be submitted for inclusion in the record are certainly welcome.

Our first witness is Adm. Harold Shear, Maritime Administrator of the Department of Transportation.

I do have an opening statement from Senator Inouye which will be included in the record as if read in full at this point.

[The statement follows:]

OPENING STATEMENT BY SENATOR INOUYE

Pending the administration's recommendations for a revitalized maritime program, we must at least "hold the line" against any further decline of our merchant marine which is now in serious trouble.

Although the administration has been studying this problem for over a year, its recommendations have not been forthcoming as yet.

I therefore wish to commend the distinguished chairman of our subcommittee and the cosponsors of S. 2336, for taking the initiative and introducing legislation to authorize funding for some of the existing maritime programs. It is quite difficult to do more than recommend a "holding action" until such time as Congress has at least had the opportunity to consider the long term proposals of the administration.

For the second consecutive year, no funds have been requested for our major shipbuilding program—construction differential subsidy. The vacuum that exists as a consequence has not only seriously threatened our shipbuilding and ship repair base, it also has prevented our subsidized merchant fleet from acquiring the new vessels it needs to compete successfully in our international trades.

These problemss are further exacerbated by a failure to increase the statutory ceiling for another highly successful program—title XI loan guarantees; and an effort to impose a limitation on the amount of the guarantee authority which remains.

Simply stated the Title XI program does build ships; does not cost the Government any money; and does not distort the credit market.

In an effort to deal with the need of U.S.-subsidized operators for new vessels, S. 2336 would permanently authorize them to build and reconstruct in foreign shipyards.

While I can appreciate that this provision is born of necessity, I have serious misgivings whether it is in the best long-term interests of our maritime industry and our national security.

To make such a major and permanent change in our maritime policy without thorough and intensive study and investigation, including consideration of alternatives, seems precipitous to me.

Under present circumstances therefore, we are faced with a dilemma which however difficult must be resolved, if only temporarily.

I would hope that the testimony today will help us reach an accommodation which, I believe, we would all agree is only an interim solution.

STATEMENT OF ADM. HAROLD E. SHEAR, MARITIME ADMINISTRATOR, DEPARTMENT OF TRANSPORTATION

Admiral SHEAR. Good morning, Mr. Chairman.

I have a statement which I would like to submit for the record and at the same time read you a brief summary statement in lieu of the longer submitted statement, if I may, sir.

Senator GORTON. Fine. Go right ahead.

Admiral SHEAR. Mr. Chairman, I am glad to appear before you this morning to present the Maritime Administration request for appropriations for fiscal year 1983.

I would like to say that the U.S.-flag share of the Nation's foreign-trade liner cargo tonnage is not increasing. It is dropping. It has fallen from 30.9 percent in 1976 to 26.5 percent in 1980. We have not been that low since 1973.

Only 3.6 percent of the total tonnage moving in U.S. foreign trade is carried by our ships. Other maritime nations carry significantly more of their trade; for example, the Soviet Union, more than 50 percent; Great Britain, 32 percent; Japan, 39 percent; and Greece, 48 percent. Obviously, as the world's greatest trading nation, we have a long way to go in increasing the strength of our merchant marine.

The President's 1983 request for the Maritime Administration would provide for continued support of the maritime industry while alternate programs are being developed.

We are again proposing modest appropriation levels as follows. For the ship construction subsidy, as for 1982, no appropriation is proposed. For operating differential subsidy, an appropriation of $454 million is requested, reflecting an increase of some $37 million over 1982. For research and development, a total of $16.8 million is proposed, and this request includes $5.3 million for operation of the Coast Guard icebreaking vessels. For operations and training activities, $71 million is proposed.

In the area of ship construction the administration's review of maritime policies is addressing a variety of shipbuilding issues and potential initiatives. Meanwhile, no appropriation is requested for ship construction subsidies. It is proposed that $10 million in current budget authority, which is available from prior year appropriations, be deferred into 1983 to cover essential engineering changes and other costs associated with the completion of subsidized construction and conversion work that is underway.

For operating-differential subsidies, the administration intends to meet its obligations under existing operating differential subsidy contracts. The appropriation request for operating differential subsidies totals $454 million. This includes an increase of some $37 million over 1982.

The request for research and development amounts to $16.8 million and, as I noted a moment ago, this includes $5.3 million which was formerly included in the Coast Guard icebreaker budget but which MarAd, as a user agency, expects to pay for in the future. After the noted $5.3 million is subtracted, the remaining $11.5 for MarAd's regular R. & D. program is some $3 million above the appropriation level enacted in the fourth continuing resolution.

The request for operations and training amounts to $71 million, which is $3.8 million less than the amount authorized for 1982; $17.2 million is included for the U.S. Merchant Marine Academy at Kings Point, N.Y., $10.6 million is requested for financial assistance to the six State marine schools which are located in California, Texas, Michigan, New York, Massachusetts, and Maine; $1.6 million is requested for additional training activities; $6.5 million is requested for the national defense reserve fleet. Finally, $34.8 million is requested for other operations and training expenses.

The administration is proposing appropriations limitations for 1982 and 1983 on new commitments for title XI loan guarantees. These amount to $675 million and $600 million respectively. These reduced levels are consistent with the administration's efforts to control the volume of federally assisted credit programs.

This concludes my summary statement, Mr. Chairman. I will be glad to answer any questions that you may have.

Senator GORTON. Admiral, we understand that certain MarAd proposals have been sent to the Secretary for review and that whatever he approves may have to go to a cabinet council review after that.

First, can you give us any indication as to what possible content may come out of that process and, second, when that process will be completed?

Admiral SHEAR. We have been working vigorously for a number of months to put together a program which we consider to be appropriate for the Presidential maritime policy. We are in the final stages of completing that within the Department of Transportation, and we will be submitting it to Secretary of Transportation Lewis for his review.

Senator GORTON. He hasn't seen it yet?

Admiral SHEAR. He has not seen it yet. We are in the process of final review within the Department and submitting it to him for his final review and approval.

Senator GORTON. Can you give us a preview of what is in it at this stage?

Admiral SHEAR. I think it would be inappropriate for me to go into the details of the program at this time, sir, since they have not yet been made public.

Senator GORTON. When do you expect that the Department will complete that process?

Admiral SHEAR. I think we can anticipate within the next several months.

Senator GORTON. Before the end of this Congress?

Admiral SHEAR. Yes, sir.

Senator GORTON. Sufficiently before the end of this Congress for us to be able to do anything about it?

Admiral SHEAR. I hope so.

Senator GORTON. Well, it will have to be in less than the next several months for that to be the case. As a practical matter, if you haven't completed it by the end of next month it would be almost impossible for Congress to do anything about it this year, Admiral. I would hope that you will do everything you can to speed up that process.

Admiral SHEAR. I understand, sir. Both Secretary Lewis and I expected to have a program moving forward earlier than this. The typical problems of Washington have moved the program somewhat slower than we had anticipated several months ago.

Senator GORTON. We have been a little bit slower than we had hoped on some of our progress as well, but we really do need to speed this one up before we can get anything accomplished.

Admiral SHEAR. I understand.

Senator GORTON. In your written testimony you express no view about the provision in the bill which is before us to permit ODS operators to build abroad. Can you tell me whether or not you think that is an appropriate or a necessary provision?

Admiral SHEAR. That is a scenario which we have been reviewing very thoroughly in regard to putting our present program together. I don't think I should comment on it specifically at the moment except to say that we are reviewing that particular aspect in great detail.

Senator GORTON. In the case of this policy, of course, we have got to make up our minds on it in the immediate future in time for markup of this bill. So if the Department of Transportation is going to play any role in that determination, that decision at least is going to have to be made in a period of days or just a couple of weeks rather than several months.

Admiral SHEAR. I understand, sir.

Senator GORTON. In the absence of CDS funding do you expect the Navy budget to cover costs of national defense features? Are you working with the Navy in this regard?

Admiral SHEAR. We have been working with the Navy very closely on the subject of national defense features, as well as the readiness of the Reserve fleet. As a matter of fact, I personally had a discussion with the Secretary of the Navy on this subject just within the past several weeks. There are certain things that the Navy is prepared to do with regard to updating the status of the Ready Reserve fleet, as well as providing for defense features for new construction.

Senator GORTON. Are you working with the Navy to solve the difficulties facing operators who expect to trade in ships this year?

Admiral SHEAR. Yes, we are. That is included in our discussions at present with regard to updating the status of the Ready Reserve fleet and the need to have a reasonable amount of money to accomplish this purpose.

Senator GORTON. On another subject, to what do you attribute the fact that there is almost a $37 million increase in ODS funding required to maintain the same contracts as are now in force?

Admiral SHEAR. That is largely due to the backlog of payments for prior year activity, which we are vigorously working to clean up. There is a backlog that goes back as far as 3 to 4 years on cases that have got to be completed and settled. That sum of $36 million is largely for cleaning up those prior year outstanding cases.

Senator GORTON. Can you identify any changes, administrative or legislative, in your study designed to reduce ODS obligations on existing contracts?

Admiral SHEAR. The administration, of course, is going to honor all existing contracts. At the same time, there has not been a thorough ODS review since 1970. In the process of putting together an overall promotional program for the merchant marine, we are looking at the ODS program in some detail. Any modifications or changes which might be made, however, would be made of course, with the concurrence of the operators, as well as the concurrence of the Government.

Senator GORTON. Are you studying either mandating reduced manning levels or funding labor costs other than wages on a different basis than is presently the policy?

Admiral SHEAR. We are looking at a number of issues and I don't think it would be appropriate for me at this time to go into specifics. This issue of manning levels, however, is something that we have got to address as we modernize the merchant marine. We are faced today with relatively inefficient steam-turbine-powered ships, whereas most of our world competition is operating with much more efficient diesel powered ships. As we improve the merchant marine, we have got to ensure that our additions are the most efficient ships which we can acquire.

Senator **Gorton**. Do you have any comments on the provisions of sections 5 and 6 of the bill which we have introduced to give MarAd more flexibility in responding to defaults of title XI loan guarantees?

Admiral **Shear**. I have gone over those very carefully and there isn't any question that those provisions would give the Secretary of Transportation more flexibility than he has at present. They have not, however, been reviewed with regard to a formal Administration position and I don't think it would be appropriate for me at this time to make any further statement.

Senator **Gorton**. I will give you one more such question. You acknowledge the administration position that title XI should be subject to annual limitations and appropriation acts and set a $600 million level for 1983. What is your own reaction to our decision to hold the limit to the 1982 figure of $75 million more than that and to do so in an authorization bill?

Admiral **Shear**. Well, I am working within the $600 million limit, and I propose to work within that limit. What I have done, however, to spread that money around as realistically as possible, is limit the guarantee percentage to 75 percent in each particular case.

Senator **Gorton**. You are sort of constrained in the answers that you are able to give us here today, aren't you, Admiral?

Senators Inouye and Long may have written additional questions for you.

I do wish to urge that you do everything you can to speed up the process of review within the administration. It is especially important that you get even a tentative decision on some of those aspects which are simply going to be addressed in this bill as quickly as possible.

With that, I thank you for being with us.

Admiral **Shear**. I understand this, sir. Let me assure you again that we are working vigorously to pull this entire program together and I understand the urgency of all aspects.

[The statement follows:]

Statement of Adm. Harold E. Shear, Maritime Administrator, Department of Transportation

Mr. Chairman and members of the committee: I am glad to appear before you this morning to present the Maritime Administration (MARAD) request for appropriations authority for fiscal year 1983.

In the year since you last heard MARAD budget testimony, there have been some very significant changes in MARAD's situation. The transfer from the Department of Commerce to the Department of Transportation was accomplished last August. When he announced the transfer, the President made it clear that his designated spokesman on maritime matters was Secretary Lewis. I am proud to represent the Secretary here today, and I want to take this occasion to affirm our commitment to the declaration of national maritime policy that is set forth in section 101 of the 1936 Act as amended.

Before going into the details of our proposed authorizations bill, I would like to direct your attention to the status of the merchant marine.

The U.S.-flag share of the nation's foreign trade liner cargo tonnage is not increasing. It is dropping. It has fallen from 30.9 percent in 1976 to 26.5 percent in 1980. We have not been that low since 1973. Only 3.6 percent of the total tonnage moving in U.S. foreign trade is carried by our ships. Other maritime nations carry significantly more of their trade—Soviet Union, 50 percent; Great Britain, 32 percent; Japan, 39 percent; and, Greece, 48 percent. Obviously, as the world's greatest trading nation, we have a long way to go in increasing the strength of our merchant marine.

The problems we face today did not appear overnight, and they won't be easy to solve. Nonetheless they must be solved if we are to turn this industry around. To this end, we are devoting a major effort to the formulation of a new program. Every approach we have been able to come up with, plus every concept that has been put forth by the industry, is being thoroughly reviewed. It is still too early to say just what the program will look like. However, I can assure you that we are working very hard to come up with a program that will provide to the maritime industry the boost it so sorely needs.

The President's 1983 request for the Maritime Administration would provide for continued support to the maritime industry while alternative programs are being developed. We are again proposing modest authorizations levels, as follows:

For Ship Construction Subsidy—as for 1982, no appropriation is proposed.

For Operating-differential Subsidy—an appropriation of $454,010,000 is requested, reflecting an increase of $36,862,000 over 1982.

For Research and Development—a total of $16,800,000 is proposed. This request includes $5,300,000 for operation of Coast Guard icebreaking vessels. The Subcommittee on Coast Guard and Navigation has recommended that user agencies such as MARAD fund these vessels instead of Coast Guard.

For Operations and Training activities—$71,013,000 is proposed. This includes $29,607,000 to cover maritime education and training expenses; $6,516,000 for reserve fleet expenses; and $34,890,000 for other operations and training expenses, including most of our personnel and overhead costs.

SHIP CONSTRUCTION

The Administration's review of maritime policies is addressing a variety of shipbuilding issues and potential initiatives. Meanwhile, no appropriation is requested for Ship Construction Subsidies. It is proposed that $10,000,000 in current budget authority, which is available from prior year appropriations, be deferred into 1983 to cover essential engineering changes and other costs associated with the completion of CDS construction and conversion work that is now underway.

OPERATING-DIFFERENTIAL SUBSIDIES

The Merchant Marine Act of 1936 provides that operating subsidies be paid equal to the differential between certain U.S. and foreign ship operating costs. The Operating-differential Subsidy program puts the operator on a breakeven basis for wages, maintenance and repair, some insurance costs, and, for some vessels, subsistence.

The Administration intends to meet its obligations under existing Operating-differential Subsidy contracts. The appropriation request for Operating-differential Subsidies totals $454,010,000. This includes an increase of $36,862,000 over 1982. Of the total, $366,771,000 will be used for current subsidy payments, which will cover 151 ships in 1983. The remaining $87,239,000 will be devoted to the payment of costs of earlier year operations and will enable us to make substantial progress toward the elimination of prior year payment backlogs.

The outlays for current year operations reflect an increase in fleet activity plus changes in the cost of operations. The increase in fleet activity over the 1982 level accounts for $4,615,000. This increase represents a return to normal operations from early 1982, when more ships than usual were in idle status. Other changes will yield a net increase of $270,000, which places the current year increase at a total of $4,885,000. Outlays for the final payment of prior year costs are necessary because of the three years required for the final collection of accurate foreign and domestic cost data. The budget request of $87,239,000 for prior year payments includes an increase of $31,977,000 over the 1982 level of prior year payments.

RESEARCH AND DEVELOPMENT

The Maritime Administration's research program works on ways to make industry more productive and reduce its costs. It addresses problems common to U.S. operators or shipyards, and it implements the results among the various firms. The accomplishments have been significant and cooperative research will be one part of our efforts to return the industry to a competitive position in World markets.

The request for Research and Development amounts to $16,800,000. As I have noted, this includes $5,300,000 which was formerly included in the Coast Guard icebreaker budget but which MARAD, as a user agency, expects to pay for in the future. The MARAD program has collected data on ice conditions in the Arctic for several years using Coast Guard vessels. Tankers are one of the transportation options for the extensive oil and gas resources in the area. According to a recent study, this area could contain 50 percent of all U.S. reserves. The Arctic R&D project in question, which is jointly conducted by MARAD, the Government of Canada, and the State of Alaska is developing a statistical base for commercial tanker construction decisions.

After the noted $5,300,000 is subtracted, the remaining $11,500,000 for MARAD's regular R&D program is $1,009,000 more than the amount authorized in the Reconciliation Act of 1981, and $3,009,000 above the appropriation level enacted in the Fourth Continuing Resolution.

The $11,500,000 level would fund several projects of immediate importance, including: 1) work on fuel efficient power plants; 2) upgrading shipbuilding practices; 3) automation of ship operations; and 4) increased market analysis and sealift readiness.

The increase of $3,009,000 from the 1982 level includes $574,000 for improvements in the use of diesels on US ships and in the safe burning of coal in a new generation of ships. Another $1,135,000 of the increase will go toward further automation of operations such as cargo booking, additional human factor research, and increased research on ports and cargo handling. In addition, $700,000 of the increase is requested for more market analysis and for further design efforts to make commercial ships more adaptable to national defense needs. The final $600,000 of the requested increase would be used to begin the replacement of various obsolete components of the Computer-Aided Operations Research Facility (CAORF), which was built at Kings Point in 1974.

OPERATIONS AND TRAINING

The request for Operations and Training amounts to $71,013,000, $3,885,000 less than the amount authorized for 1982.

The $17,251,000 is included for the United States Merchant Marine Academy at Kings Point, New York. This includes $1,406,000 to cover increases in Academy operating expenses. However, this increase is more than offset by the elimination of the Kings Point facilities modernization program, consistent with the President's program to reduce Federal expenditures for nonessential work.

The $10,668,000 is requested for financial assistance to the six State marine schools, which are located in California, Texas, Michigan, New York, Massachusetts, and Maine. This includes $600,000 for direct payments to the schools, $2,600,000 for student incentive payments, and $7,468,000 for the maintenance and repair of schoolships.

The $1,688,000 is requested for Additional Training activities. This is the same amount as the 1982 authorization less anticipated savings resulting from the transfer of two of the radar schools to private auspices.

The $6,516,000 is requested to cover National Defense Reserve Fleet costs. This account shows a net decrease from last year of $1,489,000, attributable primarily to the exclusion of certain one-time costs that were provided for in 1982.

Finally, $34,890,000 is requested for other Operations and Training expenses. These funds provide for program costs, including most agency personnel and overhead costs, plus direction and administration of several agency activities. An increase of $1,681,000 is attributable to increased operating costs.

FEDERAL SHIP FINANCING PROGRAM

The Administration's proposed bill includes a new provision which would require that annual limitations on loan guarantee commitments be included in the appropriations acts.

The Administration is proposing appropriations limitations for 1982 and 1983 on new commitments for loan guarantees. These amount to $675,000,000 and $600,000,000 respectively. These reduced levels are consistent with the Administration's efforts to control the volume of Federally assisted credit programs. It is estimated that the resulting balance of commitments and guarantees in force at the end of fiscal year 1983 will amount to $8,710,000,000. This is well within the current $9,500,000,000 statutory limitation on outstanding MARAD guarantees.

Finally, as a technical matter, the Administration's bill does not include a provision to authorize additional amounts for pay increases. This is consistent with other authorizations bills, such as Coast Guard, which do not contain this provision.

This concludes my prepared statement, Mr. Chairman, and I will be glad to answer the Committee's questions.

[The following information was subsequently received for the record:]

Questions of Senator Inouye and the Answers Thereto

Question. According to previous MarAd testimony, for the remainder of the 1980's, U.S.-subsidized operators will have obligations under the law to replace older vessels. (a) Since no CDS is requested, there will be no funds available to assist the operators meet their legal obligations, will there? What does MarAd plan to do?

Answer. The ship operators who are signatory to ODS agreements are contractually bound to replace their vessels at the end of their economic lives, 25 years in the case of liners and 20 years in the case of bulk ships. Replacement vessel(s) must be contracted for with sufficient leadtime to permit the commencement of operation by the replacement when the original vessel is retired. The standard leadtime allowance is 3 years. In years other than 1982, and possible 1983, it has been required that ODS-supported ships be U.S.-built.

The issue of ship replacement is one that is currently being examined in context of the overall maritime policy review. The options actively under consideration include the build foreign provision currently authorized by the 1981 Reconciliation Act. Under the terms of the 1981 Reconciliation Act, set forth as section 615 of the Merchant Marine Act, 1936, foreign-built ships acquired in 1982 will be eligible for ODS, and the same will be true in 1983 if there is a CDS appropriation of at least $100 million or a program that provides equivalent shipbuilding incentive.

Subsidized ship replacement is among the issues that are being addressed in the development of the administration's maritime policy proposals.

Question. CDS funds are not only used for ship construction, they are also used for conversion; for trade-ins against new construction; for change orders, etc.

Last year, you may recall, no new CDS funds were requested, but there was some money available which had been deferred.

Congress was then put in the middle, as two carriers each sought to get first chance at the remaining funds.

Obviously one carrier was ultimately satisfied; and the other felt it had been disadvantaged.

(A) There are no CDS funds requested for fiscal year 1983. I understand, however, one carrier may seek to have some CDS funds added specifically to enable it to trade-in old vessels against new ship construction.

If this report is accurate, doesn't it point up the problem of not having a maritime policy? In other words, you have a situation where individual ship-operators have to come to Congress seeking special assistance on an ad hoc basis. And if Congress authorizes money in one case, the other operators are disgruntled.

Answer. Competition for CDS assistance is not unique to fiscal year 1981 and fiscal year 1982. Even in years of substantial budgetary commitments for shipbuilding, CDS applications have often exceeded available funds.

Under such circumstances, it is necessary to consider not only the statutory criteria for CDS eligibility, but also achievement of the objectives of the Merchant Marine Act within budget constraints.

The Administration is actively pursuing alternative financing that would provide funding for ship trade-ins.

Question. Both S. 2336, and the administration's budget request propose a $675 million limit for fiscal year 1983 on loan guarantees under title XI, even though about $1.5 billion of authority remains under the ceiling in existing law ($12 billion).

Moreover, the title XI applications presently on file at MarAd request a total of about $3.5 billion in loan guarantees. (A) My question is: On what basis did the Administration decide that $675 million was an appropriate limit on Title XI guarantees for fiscal year 1983? Did MarAd or OMB do any kind of economic or budgetary analysis to determine if there should be a limit; and if so, that it should be $675 million?

Answer. Under the provisions of the Omnibus Reconciliation Act of 1981, the Maritime Administration's portion of the total $12 billion title XI guarantee program is $9.5 billion. Even without the imposition of annual ceilings, the remaining amount of statutory authority precludes funding of all the applications on file.

The administration proposed annual limitations for fiscal year 1982 and fiscal year 1983 of $675 million and $600 million, respectively. As part of its effort to reduce the size and effect of Government involvement in the credit markets that lead to market distortion and to control the volume of federally assisted credit programs, ceilings are necessary on all loan and guarantee programs if effective control is to be achieved.

In reviewing the title XI program to determine the appropriate level of financing for 1983, the administration took into consideration the fact that much of the demand for title XI had shifted from deep draft vessel to offshore support vessels, drill rigs and tugs and barges. It is the administration's view that only the deep draft vessels are at a competitive disadvantage with foreign vessels and that is the segment of the industry where the emphasis ought to be placed.

Question. I understand MarAd has recommended to the Secretary of DOT several "near term initiatives" for a maritime promotional program.

Specifically: Presidential Statement on Cargo Preference Laws: This would tighten the application of these laws and ensure compliance by federal shipping agencies.

Bilateral Maritime Agreements: Cargo sharing agreements would be encouraged with those United States trading partners desiring such agreeents.

Regulatory Reform for Shipbuilding and Ship Operations: A government/industry panel would review federal regulations to identify those which inhibit efficiency or restrict competitive capability.

Extension of the Jones Act to the Virgin Islands Petroleum Trades: Shipments between the Virgin Islands and other U.S. points would have to move on U.S.-flag vessels. (A) Would these initiatives require legislation? (B) Other than the last initiative I mentioned, would any of them really have "teeth", or are they more cosmetic?

Answer. We believe that the initiatives you cite, with the possible exception of the last one, could be implemented without new legislation. There are divergent legal opinions as to whether the President can eliminate the Virgin Islands Jones Act waiver selectively, as for oil, without legislation. This issue would have to be resolved before that initiative was undertaken.

These measures, if property implemented, could achieve a positive impact on the U.S. shipbuilding and ship operating industries. A Presidential statement reaffirming the requirement for compliance with existing cargo preference laws would be useful in assuring the availability of cargo to U.S. operators. Bilateral cargo sharing agreements offer the potential for improving carriers' load factors and freight revenue in cases where there are artificial barriers to U.S.-flag participation in the carriage of our foreign trade.

An initiative to review and streamline regulations affecting the maritime industries would be helpful in identifying and reducing any unnecessary costs and restrictions on flexibility which decrease the potential of U.S. firms to match lower cost foreign competitors. Unnecessary or overly burdensome regulations can distort the marketplace and may cause industry dependence on government assistance.

Question. I understand a subsidized operator is trying to get funds from MarAd by trading in three vessels, and applying the funds towards acquisition of three vessels under construction. This would require an amendment authorizing $25 million in CDS funds for that purpose. Is MarAd opposed to this?

Answer. MarAd has negotiated vessel trade-ins in conjunction with contracts for vessel replacements built under the CDS program. The primary concern has been the maintenance of the fleet's delivery capacity and military support capability. In an application dated June 30, 1981, American President Lines, Inc. requested permission to trade in three C6 containerships, the *President Polk, President Truman,* and *President Kennedy* for $25 million. The proceeds were to be applied to the purchase of three C9 containerships which were under construction at the Avondale Shipyard.

This request was denied due to lack of sufficient construction-differental subsidy funds. I can not support an amendment that would authorize $25 million in CDS funds for this purpose because the administration is actively pursuing alternatives that would provide for the trade-in of the APL ships.

Question. Over a year ago, the subcommittee submitted to the Administration a detailed list of questions regarding our shipbuilding capability; whether our CDS program should be changed, and if so, how; and if our tax incentive policy for shipbuilding should be changed.

These questions touched on fundamental issues involved in formulating maritime policy.

To date, of course, the Administration has not answered these questions because it still is studying the options for a maritime policy. (A) Insmuch as these issues are still under study, don't you think it would be premature for the Administration to support a permanent provision to build foreign, or to permit CCF funds to be used to build foreign?

Answer. This is one of the issues we are examining at this time. It would not be appropriate for us to comment until our policy review is complete.

Question. For the past 2 years, the Administration has said that its 5-year naval shipbuilding program will be sufficient to sustain our shipyards. I would like you to comment on a major article which appeared in the N.Y. Times, (April 11, Sun. Ed.). In part, it read:

"Congressional skeptics, conservatives and liberals alike, have pointed out that rarely in the past have 5-year shipbuilding plans come to pass. It is relatively painless for an administration, they said, to ask for a few ships for the coming year and to leave the bulk of a shipbuilding program for later years." The Reagan Administration has followed that pattern in its planning so far.

Answer. It is inherent in the nature of well-balanced five year procurement plans that they call for roughly equivalent obligations in each year, with the result that the sum of the out-year projections generally exceeds the current-year request by a factor of about four, all other things equal. This administration's plan is a rational 5-year plan, and it does in fact spread its ship procurement total over the planning period.

Question. CASO has suggested that an amendment be added to the fiscal year 1983 authorization bill which would allow foreign constructed or reconstruced liner vessels to participate in the domestic trade between Hawaii and the mainland as part of a foreign voyage provided that the foreign vessel operator pay to the Secretary of Transportation a pro rata portion of the foreign/U.S. cost differential. This payment, theoretically, will create cost parity between foreign-built and U.S.-built ships.

In addition to further eroding of the Jones Act, wouldn't the CASO proposed amendment operate to the disadvantage of the operator of domestic vessels because the cost differential premium does not take into account the payment of interest calculated on the entire unamortized foreign/U.S. cost differential attributable to the domestic portion of the voyage? At today's vessel costs and high interest rates, interest is a substantial cost factor.

Answer. Unless accounted for in the payback terms, the interest cost differential you ascribe to foreign-built vessels would exist. Even with payback of a pro-rata portion of the foreign/U.S. cost differential, the entry into the domestic trade of foreign-built U.S.-flag vessels enjoying such an interest cost advantage would place U.S.-built, domestic vessels at a disadvantage.

Question. Is it your understanding that nothing in S. 2336 would permit U.S. ships which are built foreign to carry cargo between Hawaii and the mainland as part of a foreign voyage?

In other words, the Jones Act exception in Section 506 of the Merchant Marine Act of 1936, would not apply to U.S.-flag ships built foreign under the provisions of S. 2336?

Answer. Nothing in S. 2336 would permit the operation of foreign-built, U.S.-flag vessels in the carriage of cargo between Hawaii and the mainland as part of a foreign voyage.

Section 506 of the Merchant Marine Act of 1936 precludes the domestic operation of vessels built with construction differential subsidy [DS] except under certain circumstances including calling on Hawaii as part of a voyage in the foreign trade. These exceptions include provisions that there be pro rata payback of CDS.

These exceptions to the general prohibition against the domestic operation of CDS-built vessels in no way affects Section 27 of the Merchant Marine Act of 1920 (the Jones Act) which requires that all cargo carried between points in the United States, its Districts, Territories, and possessions be on vessels owned by U.S. citizens and built in and documented under the laws of the United States.

Likewise, the provisions of S. 2336 which would deem vessels built in foreign yards under Section 615 to be U.S.-built for purposes of qualifying for operating subsidy and preference cargoes in no way affect the requirements for participation in domestic trade.

Question. I note that DOT has recently established a martime advisory committee made up of users, carriers, builders, etc. (A) When will this committee meet? (B) Will it have an opportunity to review and make recommendations on the administration's maritme proposals before they are set in concrete?

Answer. The advisory committee is expected to meet early this summer. Thereafter, the committee will periodically at my request. The members comprise a cross section of the maritime industry, including ship owner and operators, shippers, shipyards, and labor representatives. Members will serve one year terms, without compensation. It is expected that recommendations made by the Committee will provide a focus for priorities and approaches for the maritime program.

Question. (A) Do you believe that over the years the title XI program has been a good one, i.e., it builds ships?

(B) Isn't it accurate to say: That Title XI contributed significantly to the national defense.

That the administrative expenses of title XI are paid by the users of the program, so that no part of those expenses is borne by the government?

That there are no direct budget outlays. (1) title XI operates independently of the Federal financing bank; (2) there is no direct borrowing by the Treasury.

That the Treasury has never been called upon to "make good" a guarantee under title XI; and there is little likelihood it ever will be.

(C) In view of the foregoing, what is objectionable about the Title XI program?

Answer. The Federal Ship Financing Guarantee (title XI) Program has been in effect since 1938 and is one of the oldest and most successful government guarantee programs. Since its inception, the program has assisted in financing the construction of over 5,000 vessels with a total construction cost exceeding $10 billion.

The title XI program contributes to our national maritime objectives primarily by fostering construction orders that help maintain the shipbuilding mobilization base. The program is designed to be self supporting. Initial filing and investigation fees along with yearly guarantee fees, go into a revolving fund which is used to pay all expenses, including salaries, associated with the program. This revolving fund also provides the funds needed to pay principal and interest on title XI obligations in the event of a default. In the past this revolving fund has paid all operating expenses and default costs.

The program has not generated any direct budget outlays and typically produces offsetting receipts that contribute to reducing net outlays. Guaranteed loans are placed directly in the private capital markets by vessel purchasers and their underwriters. No Federal funds are loaned via the Federal Financing Bank. The program has never had to exercise authority to borrow from the Treasury.

The administration does not consider the program inherently objectionable. It believes that the focus of the program ought to be deep draft vessels in the foreign trade, that segment of the industry that is at a financing disadvantage with foreign competition. The administration is also concerned about and seeks to control the combined effect of all Federal loan and loan guarantee programs on the private credit markets. The establishment of effective control requires the adoption of ceilings on all such programs however meritorious.

Question. The Merchant Marine Act of 1936 states the U.S. must have a merchant marine capable of serving as a naval and military auxiliary in times of war or national emergency. In your opinion, will today's privately-owned, privately-operated merchant marine meet the sealift requirements of the Department of Defense if a national emergency were to develop? (a) If it cannot meet the needs of the Department of Defense, what is the administration doing to provide a merchant marine capable of serving as a naval and military auxiliary.

Answer. Augmentation of the U.S.-flag fleet by some 400 European NATO-flag ships has been arranged to provide for the timely deployment and resupply of U.S. forces in a NATO war. The U.S.-flag fleet done is clearly not adequate for that purpose. Contingencies in which the United States cannot rely on allied shipping assistance are not as demanding as the NATO case, and sufficient numbers of ships can be made available from the merchant marine to meet deployment and resupply needs in conjunction with Military Sealift Command ships and vessels from the National Defense Reserve Fleet (NDRF). The administration is now supporting the expansion of the Ready Reserve Fleet component of the NDRF to improve U.S. sealift capability applicable in the early stages of contingency deployment. In addition, the subject of sealift is being addressed in the deployment of maritime program proposals.

Question. Do you believe that our present cargo preference laws are adequate to ensure that 50 percent of Government-impelled cargo moves on U.S.-flags? Have you had any difficulty getting agencies to observe the 50/50 requirement?

Answer. The cargo preference laws are generally effective in providing adequate U.S.-flag carriage of the various cargoes encompassed by the laws. At times, there have been different interpretations concerning the applicability of the statutes. However, we are working closely with the various agencies to overcome any differences and to assure that U.S.-flag vessels carry the mandated share of Government-impelled cargo.

Senator GORTON. Thank you.

Chairman Green.

Welcome, Alan, you may proceed.

STATEMENT OF HON. ALAN GREEN, JR., CHAIRMAN, FEDERAL MARITIME COMMISSION, ACCOMPANIED BY JAMES K. COOPER, MANAGING DIRECTOR; FREDERICK F. TRUTKOFF, DIRECTOR OFFICE OF BUDGET AND FINANCIAL MANAGEMENT; AND ROBERT BOURGOIN, DEPUTY GENERAL COUNSEL

Mr. GREEN. Thank you, Mr. Chairman.

Good morning, Mr. Chairman and members of the committee. I welcome this opportunity to appear before you to discuss the budget authorization of the Federal Maritime Commission.

Accompanying me today are Mr. James K. Cooper, the Commission's Managing Director; Mr. Robert D. Bourgoin, our Deputy General Counsel; and Mr. Frederick F. Trutkoff, Director of the Office of Budget and Financial Management.

Mr. Chairman, at the outset I would like to briefly outline for the committee the major functions and statutory responsibilities of the Federal Maritime Commission. As you know, the regulation of the liner shipping industry in the foreign commerce has never been as comprehensive as the regulatory schemes governing the surface-and-air transportation industries.

The Shipping Act does not authorize the Federal Maritime Commission to control entry or the levels of rates or service in the U.S. foreign commerce. Rates can be reduced upon filing with the Commission, and carriers are free to employ any type of vessel which they choose. The judicial, legislative, and enforcement functions of the Commission can be briefly summarized as follows:

We review agreements between persons subject to the act, which, if found to conform with the Shipping Act standards, are approved by the Commission;

We serve as the central repository of tariffs filed by ocean carriers and conferences;

We have an active enforcement program to uncover unjustly discriminatory or unfair practices;

We administer the Controlled Carrier Act of 1978 to protect ocean carriers serving our trades from any predatory rate cutting on the part of foreign-government-controlled carriers;

We serve as the forum for adjudicating disputes among carriers, ports, and shippers;

We license and supervise the activities of ocean freight forwarders;

We certify the financial responsibility of vessel owners to clean up pollution of our Nation's waters resulting from oilspills and toxic discharges; and

We certify the financial responsibility of the operators of passenger vessels to indemnify passengers for death, injury, or nonperformance.

As a supplement to this description of our programs, it may be helpful to the committee for us to present a few statistics so that you may have a quantitative explanation of our regulatory activities.

During fiscal year 1981, the Commission issued 393 final decisions. Of these, 65 were formal proceedings, 88 involved special docket applications, 222 were informal dockets involving small claims of shippers against ocean carriers; and 18 related to rulemaking proceedings.

Pursuant to the special docket procedures for waiver or refunds of overcharges, reparations of approximately $2 million were paid directly to the shippers by ocean carriers.

The Commission also settled 64 cases totaling $1 million in civil monetary penalties, primarily for the illegal rebating in the U.S. foreign commerce.

During fiscal year 1981 we collected over $2.8 million in fees and penalties. This revenue represents 24 percent of the Commission's 1981 operating expenses, which was deposited directly with the Treasury and is not reflected in our budget, but should be considered in terms of the Commission's cost effectiveness.

The Commission, through its consumer affairs program, assisted shippers in recovering more than $120,000 from persons subject to the act.

In addition, we are reviewing all of our current programs for the purpose of consolidating, paring down, and reorganizing programs wherever possible in order to develop the most effective and efficient operation possible.

We have made active use of our exemption authority pursuant to section 35 of the Shipping Act to reduce the paperwork burden on those we regulate.

We are currently in the process of conducting a review of our fee schedules to determine whether they are adequate. In connection with this review, I have also directed the staff to examine whether extension of fees to other activities and services is appropriate.

The Commission has already taken the following positive steps to achieve savings during fiscal years 1982 and 1983: The halting of promotions; elimination of all cash awards; implementation of a hiring freeze; reduction of travel expenses; reduction of FTS telephone expenses; total elimination of consulting services; elimination of outside training; reduction in fiscal services; and, reduction in office supplies.

Before I review the exact budget estimates, allow me to put those figures into perspective. The FMC budget is strictly an operating budget with 83 percent required for personnel and 12 percent for fixed costs. We administer no grant programs, and we have very limited discretionary funds. As we noted above, we also returned 24 percent of our budget to the Treasury in fees and penalties.

The OMB budget estimates for fiscal year 1983 in the amount of $10,428,000 and 290 permanent positions represent a reduction of $797,000 and 16 positions from the $11,225,000 and 306 permanent positions approved pursuant to the authority under the continuing resolution for fiscal year 1982.

From 1981 to the fiscal year 1983 projections, the Commission will have experienced a 21-percent reduction in authorized positions, from 366 to 290, and a 14-percent reduction in appropriations from $12,100,000 to $10,428,000.

In addition, we have been requested to absorb $385,000 of civilian pay raises that went into effect on October 1, 1981, and $206,000 of annual costs associated with lifting the pay cap for senior Government personnel.

The Commission has examined all available options, including the furloughing of employees, to achieve the budget reductions approved by OMB for fiscal year 1983 while insuring the most effective and efficient operations of the Commission.

The OMB fiscal year 1983 budget estimates will require the FMC to eliminate from 43 to 50 permanent positions. This represents a reduction of 14 to 16 percent from our 1982 authorized positions. More reductions would be required if the lower authorization figure of $10,378,000 contained in S. 2336 is adopted. This comes at a time when we are on the verge of obtaining significant new legislation affecting all our programs.

I strongly support the administration's attempt to reduce Federal expenditures in order to achieve a balanced budget. However, I also have a responsibility to apprise the Congress of the effects of the proposed budget estimates on the FMC's operations and its ability to carry out those programs mandated by the Congress. To that end, I have appeared today to provide you with the facts.

Mr. Chairman, this completes my prepared statement.

However, before I answer any questions I would like to make a personal remark to you, sir, that, while I have limited my testimony to the funding of the Commission under the 1916 Shipping Act, it is my hope that next year I will be testifying on our budget as it relates to S. 1593. I certainly hope that you, sir, continue to push for the speedy enactment of that bill.

I know I speak for all of us at the Federal Maritime Commission when I say that the successful passage of S. 1593 is our No. 1 priority, and, as in the past and as you so kindly mentioned earlier today, sir, we will do all we can to help you in the future on this.

I will answer any questions, sir.

Senator GORTON. Thank you very much, Mr. Chairman. We certainly see eye to eye on that.

There is an implication in your statement that you believe $10,428,000 to be inadequate funding for FMC programs. How much do you think is the minimum necessary to carry out effectively what you consider to be your responsibilities?

Mr. GREEN. I would say, sir, that the minimum, including the lifting of the pay cap and the general pay increase that went into effect in October 1981, $11,650,000 with 284 work-year permanent positions, representing 290 full-time permanent positions.

Senator GORTON. We will certainly note that in connection with your testimony.

Mr. GREEN. Thank you, sir.

Senator GORTON. That is important to us and we may ask you for more detail as to how you arrived at that specific figure on manning levels.

Mr. GREEN. We certainly will be more than happy to provide that information.

[The following information was subsequently received for the record:]

In response to your question concerning additional details as to how we arrived at the $11,650,000 representing 284 workyears for 290 permanent positions and 2 workyears for part-time positions for a total of 286 workyears, we submit the following:

	Total positions	Total workyears	Amount
Fiscal year OMB budget estimates	293	278	$10,428,000
Additional workyears required for permanent positions—9		9	247,000
Less 1 part-time position	−1	−1	
Lifting of pay cap			206,000
October 1981 civilian pay raises			385,000
Within-grades			80,000
Merit pay			30,000
Promotions			51,000
Compensation and medical benefits under the Federal Employee's Compensation Act			26,000
Overtime			15,000
ADP rental for freight forwarders, oil pollution, and agreement processing			140,000
Equipment			25,000
Miscellaneous—reporting services and training			17,000
Total	292	286	11,650,000

It must be noted that the overall difference between the fiscal year 1982 budget estimate of $11,498,000, which includes a pay supplemental of $273,000 approved by OMB, and $11,650,000 required for fiscal year 1983 is only an increase of $152,000. This increase is attributable primarily to a mandatory increase of $81,000 for office rent charged by the General Services Administration; $88,000 for personnel services, offset by a reduction of $25,000 in Travel costs. Even with 8—9 full time minus 1 part time—added to OMB estimates (278), the Commission will still experience a reduction of 15 workyears from 1982 budget (298 permanent plus 3 part time minus 15 equals 286).

Senator GORTON. You tell us that between 1981 and 1983 the Commission's authorized positions will have declined from 366 to 290. In 1981, did the Commission actually have 366 employees? What real difference, as opposed to authorized difference, are we talking about?

Mr. GREEN. No; we didn't have that many in our employment. Our actual employment was 341.

That was before my time. You know, I am just about cut to the bone.

Senator GORTON. How many employees are there right now?

Mr. TRUTKOFF. Onboard as of today?

Senator GORTON. Yes.

Mr. TRUTKOFF. 289 permanent employees and 5 part-time employee, for a total of 294.

Senator GORTON. What would that be in actual numbers if we passed, first, the budget the administration has suggested and, second, what you have asked for here in answer to my question?

Mr. TRUTKOFF. The administration's budget would reduce us to approximately 244 people.

Senator GORTON. The administration proposal?

Mr. TRUTKOFF. Yes.

Senator GORTON. What about your own? I am sorry, I think I must have missed the number that you gave me.

Mr. GREEN. The $11,650,000 will allow for employment of 292 people, which includes 2 parttime. This represents a reduction of 49 people from the fiscal year 1981 onbroad strength and a reduction of 8 people from the fiscal year 1982 onboard strength.

Mr. TRUTKOFF. In fiscal year 1983, the FMC will need 290 full-time and 2 part-time permanent positions. This amounts to 284 work-years of employment for the permanent positions and 2 workyears for part-time positions for a total of a full-time equivalent of 286 work-years. In fiscal year 1983, OMB has approved 290 permanent positions, 275 work-years for the permanent positions and 3 part-timers. So we have a total of 278 full-time equivalent in work-years approved by OMB in fiscal year 1983.

Mr. **Green**. There are two things I would like to point out very briefly.

No. 1 is that I want to recall your attention to the fact that we do raise approximately 24 percent of our operating budget and we are in the process of looking at fees which would further decrease the net cost of the FMC to the Government.

Another point is that, under the previous administration, as near as we can make out, with the lifting of the pay cap and the pay raises, our budget would be well over $13 million.

Senator **Gorton**. You mentioned at the end of your comments your desire that next year you would be testifying on the basis of S. 1593. What savings could we anticipate if S. 1593 were enacted in its present form reflecting the fact that so much of the Commission's time now goes to reviewing agreements and that prior approval is eliminated by that bill?

Mr. **Green**. Well, Senator, I wrote you a letter on February 12 that suggested the elimination of the Commission's preimplementation approval responsibilities. We have also worked very closely with the administration on this. Instead of waiting for 9 months or more, agreements could be approved in 45 days. That is where I think the savings will probably be made.

Now, as I have said many times, I don't like crystal ball gazing. However, right now your bill provides for a phasein period of 180 days. You will be happy to know that last week I appointed a blue ribbon task force within the agency to start thinking about the effects of this legislation on FMC operations and how the Commission might best respond were the bill to become law.

If it comes about, I think that on the 181st day or the first day of the new law we are going to get an awful lot of agreements coming in. So we will likely have to have quite a few people going over them. They will have to be reviewed for form and substance in order to insure that the agreements conform to all the provisions of the new law, for example, to be sure that there are no fighting ship provisions and that self-policing is included.

But once that initial rush is over, we will be able to concentrate on what we are really good at doing, and what we should be doing, and that is the enforcement of the agreements. I think the savings could most likely come about after this transition period. It would involve a reorganization of that section and perhaps a shifting of personnel. I don't think we are going to need more people in order to have an adequate enforcement program, but it is difficult to be certain, until we have a chance to operate under the new law.

Senator **Gorton**. Has the Commission considered charging fees for every agreement or every tariff which is filed?

Mr. **Green**. Yes; we are going through that now and we are looking at many different options, yes, sir.

Senator **Gorton**. When do you think you are likely to come to a conclusion?

Mr. **Green**. Well, I keep asking that question of the Managing Director. Would you like to answer that, Mr. Cooper?

Mr. **Cooper**. We have a first draft of a proposal on the user fees, Mr. Chairman. We are now in the process of going over these proposed new fees and the reevaluation of fees and I should think that we would be able to go out with a notice of proposed rulemaking on these fees in 90 days.

Mr. **Green**. Actually when the first draft came up, there were areas that needed adjustments and we sent them downstairs, if you would like to know the truth, for a little reworking.

Senator **Gorton**. Does the Commission have sufficient funding in its present budget to conduct an effective enforcement program?

Mr. **Green**. With the present budget in 1982?

Senator **Gorton**. Yes.

Mr. **Green**. Yes, sir, I think so.

Senator **Gorton**. But, nevertheless, you would increase your enforcement activities comparatively speaking if S. 1593 passed?

Mr. **Green**. Yes, sir. We would have to. I think that enforcement is our primary charge, sir.

Senator **Gorton**. Like the 1916 Shipping Act, S. 1593 authorizes the Commission to exempt any regulated agreement or activity from any requirement of the act. This may be the most powerful potential source of deregulatory efforts even after S. 1593 is enacted.

Are there still numerous burdens which, in your view, can safely be eliminated?

Mr. **Green**. Mr. Chairman, section 35 of the 1916 act has been very important in reducing the burden of regulation. In 1981 alone, the Commission took final action to exempt six types of agreements from the filing and approval requirements of section 15 of the 1916 act. You must realize that an agreement which is exempted under section 35 does not receive antitrust immunity and, therefore, the use of such exemption is limited. S. 1593 would remove that limitation.

Furthermore, the Commission has exempted certain tariff matters from the tariff-filing requirements. As for the future, if S. 1593 becomes law, the Commission will continue to review our activities and to monitor the industry for areas which would be appropriate for exemption from regulation. We don't know now how the industry will respond to a new regulatory scheme. But as we gain experience operating under the new law, the Commission will be better able to see where regulation is not beneficial. Let me assure you, that the Commission will utilize its exemption authority whenever appropriate in order to reduce the cost of regulation on the maritime industry.

Senator **Gorton**. Among the functions of the Commission are two which seem outside of its general regulatory purpose. The first is certifying financial responsibility of all vesssel operators to clean up pollution and of passenger vessel operators to indemnify passengers. Would it be more appropriate to transfer these functions to the Department of Transportation or are they most appropriately located within the Commission?

Mr. Green. Well, we have examined the pollution liability function with OMB with the idea of transferring it. It is a very important function. Frankly, nobody seemed to want it.

This is one of the areas at which we are looking to insure that it is at a cost-effective program for the Government. As far as passenger vessels are concerned, it is really a very small part of the FMC's mission. As far as the overhead to the Commission is concerned, it is a very minor element.

Senator Gorton. I should like to thank you, Chairman Green, and those who are accompanying you.

Mr. Green. Thank you, Mr. Chairman.

[The following information was subsequently received for the record:]

Question of Senator Inouye and the Answer thereto

Question. The amount of funding authorized for the FMC in S. 2336 ($10.378 million) envisions a reduction in personnel.

Under the regulatory reform bill which the committee expects to report later this week (S. 1593), ship operators will be given considerably more monopoly power because their activities will be completely immunized from the antitrust laws, and the requirement of prior FMC approval under existing law will be substantially relaxed. Prior approval, or course, is a restraint on the monopoly power of the ship operators.

Under S. 1593, the FMC cannot on its own motion stop an agreement from going into effect. It can only disapprove an agreement after it goes into effect, if it finds the agreement violates the Shipping Act.

In other words, to detect violations, the FMC will have to keep agreements under surveillance and investigation, or rely on third parties to complain.

Will you have sufficient staff to carry out your surveillance and investigative responsibilities under S. 1593?

Answer. I believe that, with our current staffing level, the Commission will be able to meet the challenges that S. 1593 presents, including the increased responsibility to monior effective agreements to ensure that they comply with the provisions of section 12 of the bill. Given the emphasis that will be placed on the Commission's enforcement and investigatory functions, we probably will require a different "mix" of people to perform those activities, but I do not believe that we will need more personnel than we currently have employed at the Commission.

The authorization level contained in S. 2336 ($10.378 million) will force substantial reductions in personnel strength. A reduction in force of over 14% may be required to reduce the Commission's spending level for fiscal year 1983 to that authorized by the bill. It is difficult to predict whether, with a reduction of that magnitude, the Commission will be fully capable of implementing the changes required by S. 1593 in the manner Congress intends. A 14% reduction in personnel will certainly have an effect on Commission enforcement with respect to agreements. With fewer resources, the Commission will conduct fewer investigations. Moreover, given the time restraints imposed by S. 1593, the ability of the Commission to complete all required investigations within the 180 days mandated will be placed in jeopardy.

Senator Gorton. We will next hear from Admiral Holloway.

I think I should announce that in about 10 minutes I am going to have to take a 15-minute break at 11 o'clock. New Senator Brady is going to be sworn in on the floor and I should be there briefly at that time.

With that, admiral, please proceed.

STATEMENT OF ADM. JAMES L. HOLLOWAY III, PRESIDENT, COUNCIL OF AMERICAN-FLAG SHIP OPERATORS

Admiral Holloway. Thank you, Mr. Chairman.

I am Adm. James L. Holloway III, U.S. Navy retired, president of the Council of American-Flag Ship Operators [CASO].

I do have a prepared statement with several attachments which I would like to submit for the record and with the committee's permission I would like to summarize that statement now in a 5-minute brief.

Senator **Gorton**. Right. The entire statement will be included in the record.

Admiral **Holloway**. Thank you, Mr. Chairman.

CASO represents the majority of U.S.-flag liner companies serving the foreign commerce of the United States. Our member companies own and operate a modern and diversified fleet of breakbulk, barge-carrying containers and roll-on/roll-off vessels. All of these ships are available under various programs for use by the United States during military emergencies.

We appreciate the opportunity to appear here today to present our views on the Maritime Administration appropriations authority request for fiscal year 1983.

Investment in and expansion of the U.S. maritime industry depends heavily on the confidence of shippers and the financial community in the Government's continuing resolve to promote a strong U.S.-flag merchant marine.

However, a series of ad hoc decisions, coupled with new budget cuts, have undermined the confidence of investors in our merchant marine. The construction differential subsidy program has been abandoned, several limits are proposed on the title XI program, a freeze on additional operating differential subsidy contracts has been imposed by OMB and a program of administrative changes to reduce expenditures under existing contracts is being implemented by MarAd.

The new ODS authorization authority request of $454 million is considered adequate to fund ODS commitments under existing contracts for fiscal year 1983.

With regard to the construction differential subsidy program, we would prefer to continue construction in U.S. yards but only if full parity with our foreign competitors is provided.

The administration has not requested additional CDS funds for fiscal year 1983 and has indicated that the CDS program is dead, at least for the foreseeable future. This action raises a vital national issue. If CDS funds are unavailable and subsidized carriers cannot build abroad, they will not be able to build or convert at all, and the U.S. liner fleet, already perilously small for national security, will decline further.

In the absence of CDS, the only possible alternative is to authorize ODS contractors to acquire, reconstruct, and repair vessels abroad. When such vessels are put into U.S.-flag operation, they must have the same rights, duties, burdens, and obligations as U.S.-built ships. We believe that this can be achieved by including an amendment in the authorization bill, such as that found in exhibit 2 of this statement.

In order to prevent a gross inequity and to prevent a CASO member to continue to operate in a trade which it has served for 50 years, our amendment makes it clear that such vessels may operate and they do now under the first sentence of section 506 of the 1936 act.

Capital cost parity, particularly during this era of high interest rates, also requires that U.S.-flag operators have relatively the same ability to finance vessels as their foreign competitors. Title XI mortgage loan guarantees are designed to provide this parity to the U.S. operator. We urge the adoption of the amendments to title XI contained in sections 3, 5, and 6 of S. 2336.

Existing law imposes a 50-percent ad valorem duty on shipbuilding maintenance and repair work performed outside the United States. We recommend that this duty be eliminated for any U.S.-flag operator not receiving a maintenance and repair subsidy.

A proviso of the foreign acquisition legislation enacted last year denied the use of capital construction funds to U.S.-flag operators building, reconstructing, or repairing vessels abroad. The effect of this action has been to reintroduce a tax bias in favor of U.S. ownership of foreign flag vessels rather than U.S. vessels. This is totally contrary to the goal of rebuilding the U.S.-flag fleet. We, therefore, recommend that the provisions of the CCF be extended to all U.S.-flag ships in international commerce.

That completes my summary, Mr. Chairman, and I would be pleased now to answer any questions that the committee might have.

Senator GORTON. You point out that the U.S. liner fleet has declined from 645 ships in 1968, close to 15 years ago, to 233 ships at the first of this year. That has not resulted in a comparable reduction in capacity or efficiency, has it? Isn't it largely because of a deliberate management policy to retire smaller, older, and less efficient break-bulk vessels and to replace them with better, newer, and more efficient vessels?

Admiral HOLLOWAY. Yes, Mr. Chairman, that is quite correct. I think that is the principal cause for the reduction in numbers of ships. The capacity is remaining essentially the same.

I would point out, however, that since 1970 the number of operators has declined from 19 to 9.

Senator GORTON. What is the reason for that? Isn't some of this due to mergers and bankruptcies of inefficient operations? Should we have attempted to keep all 19 of those in operation?

Admiral HOLLOWAY. No, sir; I don't necessarily think we should have attempted to keep every operator in business, but I do think it is an indicator of an economic fact of life. In 1970, there developed a worldwide overtonnaging; that is, there were more hulls than there was cargo to be carried.

History shows us that the foreign-flag carriers dumped their overtonnage in the U.S.-flag trades. They did this because they recognized that we were very vulnerable. That is, American-flag lines were not as competitive compared to foreign lines. One of the principal reasons of course, as you well know, Mr. Chairman, is because of Government inhibitions. We were unable to pool, rationalize, create consortia. We were under the pressures of antitrust statutes. There was no coherent cargo policy and our competition had all those benefits and none of the disadvantages.

It was that kind of pressure that enabled foreign lines to survive, when some of our lines, lines that were probably equally as efficient and capable, could not survive.

I would like to say, Mr. Chairman, that we are full supporters of your S. 1593, and we feel that this will go a long, long way, if enacted in its present form, to resolve these problems that have placed the U.S.-flag merchant fleet at such a gross disadvantage to our foreign competition.

Senator GORTON. Looking at the next 5 years or so, how many new liner vessels do you think will be added to the U.S.-flag fleet?

Admiral HOLLOWAY. Mr. Chairman, I think the answer to that question depends probably upon what happens in the next 6 months or next year. If the authority to use capital construction funds for offshore procurement is not granted, you are going to see not very many ships built for U.S.-flag operators. The reason is a very straightforward one. These would be privately-owned ships. Their acquisition is the product of corporate judgments. I don't believe these corporations are going to see funds, which were specifically set aside for recapitalization of their fleets, not be used. Or, if they do use them, to pay 2½ to 3 times as much as for a ship built abroad.

It is still a free enterprise system and I think that there just simply will not be capital investment in the U.S. merchant marine under these circumstances.

Senator GORTON. Is that what you estimate to be the difference of constructing in the United States and abroad, 2½ or 3 to 1?

Admiral HOLLOWAY. Yes, sir. The most recent figures that I have seen fall into that area.

Senator GORTON. Assuming there were no budgetary restraints, what demand would you anticipate among CASO members for new ODS contracts?

Admiral HOLLOWAY. I think that there is going to be a demand for new ODS contracts regardless of what happens in the future. If we were simply to straightline the level of activity of our U.S.-flag merchant marine into the future, we would still be adding new and reconstructed ships to the fleet and adapting the route structure to changing economic conditions. Therefore some flexibility in ODS is required for maneuvering room within the industry.

Senator GORTON. Do you believe that the amendment permanently to authorize ODS operators to build foreign should be expanded to permit them to purchase existing foreign-flag vessels and reflag them in the United States?

Admiral HOLLOWAY. Yes, sir; I do, providing those ships meet all the standards of inspection, and have all the requirements, responsibilities, and so forth of a U.S.-built ship. In other words, if acquired and reflagged, they should have both advantages and the responsibilities of a ship that was constructed in the United States.

Senator GORTON. While I am sympathetic with U.S. Lines' desire to build abroad and compete effectively in foreign trade to Asia while continuing to offer Jones Act service to Hawaii, I am not sure that your amendment protects other domestic operators servicing Hawaii. Could you explain the effect of your proposal on those operators?

Admiral HOLLOWAY. My understanding of this amendment is that it would permit U.S. Lines, which has been in that trade for 50 years, to continue in that trade. The other operators, which I understand operate under the Jones Act, would be in competition with U.S. Lines. There is no question about it.

My point is that at the present time U.S. Lines has about 10 percent of that trade on that route, and for them to continue that 10 percent does not appear to be a threat to the survival or the continued profitability of the other lines.

I would like to provide more for the record,[1] Mr. Chairman, if I may on that question.

Senator GORTON. I wish you would. I am going to have to start this break now to be down there at 11 o'clock. We will be back in about 15 minutes.

[Recess.]

Senator GORTON. Thank you for waiting, admiral. I appreciate particularly your extra time.

Can you tell me what efforts, if any, CASO operators are making with the labor leaders and their unions to reduce manning levels and labor costs? Is there any way to make that more effective in stretching out the use of ODS obligations? And, alternatively, is there anything in that area which you would recommend to us to do in connection with legislation?

Admiral HOLLOWAY. Mr. Chairman, there is an ongoing program which involves the operators and labor, which would tend to reduce ODS costs. When an operator intends to acquire a new ship, he sits down with the representatives of labor to go over the manning for that ship. As we are aware, the new ships are very highly automated, and the size of the crew can be made substantially smaller. We are seeing that in many foreign ships and those new ships that are being produced in this country. As a result of an agreement between management and labor, the new liners that are entering the fleet all have substantially reduced manning levels.

There is a secondary effect on the reduction of manpower and, therefore, ODS requirements, in that the new ships are larger and they are a great deal more efficient in their cargo-handling capability. Therefore turnaround times are reduced so that 1 single, new, modern liner can do the work of from 3 to 5 of the old break-bulks.

When one considers that you are reducing the manning of the new ships by 20 to 30 percent and they are carrying 300 percent more cargo, the result is a substantial decline in the numbers of crewmen required.

At the present time, CASO, as an organization is taking a studied look at the future of the liner industry. We think we will be able to make some suggestions as to what the future might hold, but it will be at some later date.

Senator GORTON. Thank you. We have several more questions, but because of this delay, we will submit them to you in writing.

Admiral, I thank you very much for your candid and forthright statement and answers.

Admiral HOLLOWAY. Thank you very much, Mr. Chairman.

[The statement follows:]

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[1] See exhibits 2 and 3 at p. 31.

STATEMENT OF JAMES L. HOLLOWAY III, U.S. NAVY (RETIRED), PRESIDENT, COUNCIL OF AMERICAN-FLAG SHIP OPERATORS

Good morning Mr. Chairman and members of the Committee. I am Admiral James L. Holloway III, USN (Ret.); President of the Council of American-Flag Ship Operators (CASO).

CASO represents the majority of U.S.-flag liner companies serving the foreign commerce of the United States. Our member companies own and operate a modern and diversified fleet of break-bulk, barge carrying, container and roll on-roll off vessels. All of these ships are available under various programs for use by the United States during times of military emergency.

We appreciate the opportunity to appear here today to present our views on the Maritime Administration appropriations authority/request for fiscal year 1983.

Investment in and expansion of the U.S. maritime industry depends heavily on the confidence of shippers and the financial community in the government's continuing resolve to promote a strong U.S. flag merchant marine. This is particularly true at a time when traditional western shipping nations are increasingly challenged by state supported fleets in many of the less developed nations, and state owned fleets in most communist nations. The European countries have reacted vigorously to this challenge by funneling more aid to their fleets, which they consider essential for reasons economic and national policy.

The importance of our national flag fleet was re-emphasized by President Ronald Reagan's statement in a speech given September 15, 1980, ". . . A specific naval-maritime program must be developed that will . . . restore the cost competitiveness of U.S.-flag operators in the international marketplace. It has been American policy since 1936 for the additional costs of building and operating U.S.-flag ships to be borne by a system of subsidies to help insure the competitiveness of American importers and exporters. But our parity system failed in the mid-1970's because most foreign governments moved to protect their own vital maritime interests after the shipping collapse of the mid-1970's. We must now take corrective action to make certain our merchant fleet and our shipbuilding industry survive and grow".

Unfortunately, since that statement was made, a continuing series of ad hoc decisions, coupled with new budget cuts, have further undermined the confidence of investors in our merchant marine. Instead of a comprehensive policy framework to implement the President's commitments, the Construction Differential Subsidy program has been abandoned, severe limits are proposed on the Title XI program, a freeze on additional Operating Differential Subsidy contracts has been imposed by OMB, and a program of administrative changes to reduce expenditures under existing contracts is being implemented by MARAD.

These actions are reflected in the fiscal year 1983 budget request, particularly through the elimination of all CDS funds.

These *ad hoc* curtailments of existing promotional programs are particularly unfortunate since Secretary Lewis is currently in the process of developing a new maritime promotional program for submission to the White House. The Administration's fiscal year 1983 budget message states that it, ". . . is conducting a full review of maritime policies including the need for subsidies, the importance of both the shipbuilding capability and the merchant marine to national defense, the impact of planned increases in naval shipbuilding, ways to increase commercial participation in military support functions, and the effect that new tax policies and possible trade agreements may have on improving the competitiveness of the U.S. merchant marine".

A new promotional program must challenge the industry to achieve substantial productivity increases in return for the government's renewed commitment to programs that will insure a significantly expanded merchant marine. However, it is essential to recognize that the goal of improving productivity does not imply abandonment of the cost parity concept. Increasingly, we hear statements such as "ODS costs are going through the roof" or that "the present system doesn't work". The first statement is incorrect, and the second ignores the fact that what has failed is not the concept but the implementation. Cost parity consists of three different elements: parity of operating costs, parity of capital costs and parity in the tax environment.

PARITY OF OPERATING COSTS

Our national policy has long recognized that the national defense role of the U.S. flag ships and citizen seamen dictate that the higher cost of employing U.S. seamen should be borne by the nation as a whole through a seamen's wage differential. This parity system of roughly equalizing costs of employing U.S. seamen vis-a-vis low cost foreign labor was adopted in 1936 after a number of other subsidy systems had failed.

During the past forty years dozens of Congressional and Executive branch studies have concluded that the ODS parity system is the cheapest and the most effective way of equalizing wage costs so that U.S. carriers can compete while employing citizen seamen.

Commercially, this parity concept is designed to improve rather than to burden the position of U.S. exports in international markets. Just as with national security, this consideration of our economic welfare is more important now than ever in the past. The presence of U.S. flag operators, who are primarily committed to the U.S. trades, tends to dampen rate increases which might be requested by foreign-flag operators with less commitment to U.S. economic interests. It should be noted that, properly administered, the cost parity program puts the American operator, both liner and bulk, under the same competitive pressures as foreign operators in any given trade and thus further contributes to the cost efficiency of the overall program.

The long term stability and operating cost parity provided by the present program is essential if the liner industry is to continue attracting new capital investment.

Even those who recognize that the ODS program has sustained the only viable portion of our foreign trading merchant marine often charge that ODS costs are getting out of hand. This is incorrect as you can see from Exhibit I, attached to this statement, which shows net ODS accruals in current and constant dollars for a thirty year period. Anticipated accruals in constant dollars for 1983 are the lowest in history. Further, they are only about half of the constant dollar cost for 1964. It is true that the number of subsidized liner ships has declined during this thirty year period. However, it is also true that because of increased vessel size and efficiency, particularly in turn around time, the annual ton/mile capacity of the fleet has increased. The new ODS authorization authority of $454,010,000 is considered adequate to fund ODS commitments under existing contracts for fiscal year 1983.

CAPITAL COST PARITY

The construction differential subsidy (CDS) program which was intended to give U.S. flag operators capital cost parity with their foreign competitors, failed for three reasons. First, artifical constraints on the amount of CDS that was provided for the U.S. shipyards left the American shipowner far short of capital equality with his foreign-flag competitors. Second, we did not respond to the growing role of interest rate subsidies in international shipping. Third, continuing budgetary pressures on the program resulted in such minimal appropriations during recent years that U.S. shipbuilders have not been able to benefit from the economies of scale which would have enabled them to bring down the cost of American built ships.

As we testified before this Committee last year, the members of CASO have constructed the vast majority of vessels built in U.S. shipyards for the foreign trade since World War II. We would prefer to continue such construction, but only if full parity with our foreign competitors is provided.

The Administration has not requested additional CDS funds for fiscal year 1983 and has indicated that the CDS program is dead, at least for the forseeable future. This action raises a vital national issue: If CDS funds are unavailable and subsidized carriers cannot build abroad they will not be able to build or convert at all and the U.S. liner fleet, already perilously small for national security, will decline further.

The U.S. shipbuilding industry is relatively healthy and has bright prospects. Conversely, the U.S. liner fleet has declined from 645 ships in 1968 to 233 ships at the first of this year. The number of liner companies has declined from 19 in 1970 to 9 today.

Permitting some foreign requisition, construction and reconstruction when shipyard subsidies are not available will permit the survival of the liner fleet without any major impact on shipyards.

During the past 20 years, the U.S. shipbuilding industry has experienced substantial growth (the number of workers has nearly tripled). You may hear representatives of the shipyards citing a decline in their labor force. Bureau of Labor statistics data shows that the private U.S. shipyard employment averaged 165,900 during the period 1973 through 1980. There has been a decline during the period December 1980 through December 1981 from 177,400 production workers to 175,200. This represents a reduction or decline of only 1.24 percent and, further, December of 1980 was the second highest month for production employment in U.S. shipyards during the period 1973 through 1980.

U.S. Navy expenditures in U.S. shipyards during 1981 on SCN and repair and alteration totalled $11,486.6 billion. The Administration has requested more than $23 billion for these purposes in fiscal year 1983, more than doubled over other years. SCN expenditures for the five years beginning in fiscal year 1983 are estimated in excess of $80 billion and, if estimates for repair and alteration are added to that, the total estimated U.S. Navy expenditures in U.S. shipyards over the next five fiscal years will exceed $100 billion.

The total value of work in U.S. yards has increased by 86 percent in the 8 years from 1974 to 1981.

The question really is whether our liner operators will be permitted to build at all, not whether they will build here or abroad. The shipbuilding base will not only survive but, with increased ship construction, naval and merchant ship repair, and construction of other vessels such as supply boats, methanol barges, drill rigs, et cetera, it should continue its historical growth and profitability.

U.S. operators must have a continuing ability to acquire, construct, reconstruct and repair vessels on a cost parity with their foreign competitors. In the absence of CDS, the only possible alternative is to authorize ODS contractors to acquire, reconstruct and repair vessels abroad. When such vessels are put into U.S.-flag operation, they must have the same rights, duties, burdens and obligations as U.S. built ships. We believe that this can be achieved by including an amendment in the Authorization Bill such as that found in Exhibit 2 to this statement. In order to prevent a gross inequity and to permit a CASO member to continue to operate in a trade which it has served for 50 years, our amendment makes it clear that such vessels may operate as they do now under the first sentence of Section 506 of the 1936 Act. Attached as Exhibit 3 is a detailed explanation of this.

We recommend the amendment at this time because the already heavy legislative schedule will clearly make it impossible for the Congress to consider and enact an Administration promotional program, which will be presumably sent to you sometime this Spring. As you know, present limited right to build foreign will expire on September 30th of this year. Unless this right is renewed and expanded, the U.S. flag liner fleet will be faced with inevitable and inexorable decline.

An unintended casualty of the Administration's decision not to provide CDS funds is MARAD's inability to acquire commercially obsolete U.S. flag merchant vessels for the National Defense Reserve Fleet under Section 510 of the Merchant Marine Act, 1936. Under this program, a U.S. flag operator "trades-in" vessels in exchange for an allowance of credit towards the construction or purchase of new commercial vessels. For example, one of our member companies has applications before MARAD to trade-in three type C-6 vessels against three diesel-powered containerships to be delivered later this year by Avondale shipyard.

Because Congress traditionally authorized and appropriated a lump sum for MARAD to acquire NDRF vessels *and* to provide CDS for new construction, when this Administration decided last year not to provide CDS it also failed to provide funds for the acquisition of vessels for the Reserve Fleet. This oversight was unfortunate for two reasons. First, Naval officials have testified that we need a larger Reserve Fleet and that acquiring commercially obsolete vessels is the most economical and cost effective means of increasing our sealift surge capacity. Second, MARAD's inability to acquire trade-in vessels works a great inequity on those operators who moved ahead to replace vessels in their services with modern, fuel-efficient, ships based in part on the assumption that they would be able to trade-in their older vessels against the new ships.

Capital cost parity particularly during this era of high interest rates, also requires that U.S. flag operators have relatively the same ability to finance vessels as their foreign competitors. Title XI mortgage loan guarantees are designed to provide this parity to the U.S. operator. We have reviewed a recent statement presented to the Senate Budget Committee on this subject by the Committee for Title XI Vessel Financing. We understand Representatives of that Committee will present similar testimony later today on S. 2336. We believe that the arguments which will be made in detail by that Committee completely justify the amendments to Title XI contained in Sections 3, 5 and 6 of S. 2336 and we urge the adoption of those Sections. They will discuss with you in some detail why they believe the $675 million dollar ceiling in fiscal year 1983 which is proposed in Section 4 is woefully inadequate. We endorse their position.

Existing law imposes a fifty percent ad valorem duty on shipbuilding maintenance and repair work performed outside of the United States. This duty continues the effort to force the American flag ship operator to support the ship repair industry.

We recommend that this duty be eliminated for any U.S. flag operator not receiving a maintenance and repair subsidy. In addition to the obvious linkage to the other initiatives, this will give an incentive to those operators now receiving M&R subsidy to forgo it.

PARITY IN THE TAX ENVIRONMENT

The proposed amendment found in Exhibit 2 would make Capital Construction Funds (CCF) available for foreign as well as U.S. built vessels. Most of our foreign competition pays little or no tax. Subpart F of the Internal Revenue Code recognizes this fact and provides tax parity for U.S. owners of foreign flag vessels. Capital Construction Funds (Section 607 of the Merchant Marine Act, 1936) were specifically designed to extend tax parity to owners of U.S. flag vessels. An ill conceived proviso to the foreign acquisition legislation enacted last year denied the use of CCF to U.S. flag operators building, reconstructing or repairing vessels abroad. The effect of this action has been to reintroduce a tax bias in favor of U.S. ownership of foreign flag rather than U.S. flag vessels. This is totally contrary to the goal of rebuilding the U.S. flag fleet. We therefore recommend that the provisions of the CCF be extended to all U.S. flag ships in international commerce.

Mr. Charrier of Delta Steamship Lines, a CASO member company, will follow me this morning and discuss this issue with you in more detail.

This completes my prepared statement. I would be happy to attempt to answer any questions which the Committee may have.

EXHIBIT 1

OPERATING-DIFFERENTIAL SUBSIDY NET ACCRUALS—LINER OPERATORS ONLY

[Current and constant dollars in millions]

	Current dollars	Deflator	Constant dollars
Calendar year:			
1954	106.3	[1] 89.6	118.6
1955	104.1	[1] 90.9	114.5
1956	102.7	[1] 94.0	109.3
1957	122.8	[1] 97.5	125.9
1958	140.7	[1] 100.0	140.7
1959	158.8	[1] 101.6	156.3
1960	162.7	[1] 103.3	157.5
1961	168.8	[1] 104.6	161.4
1962	174.8	[1] 105.8	165.2
1963	190.5	[1] 107.2	177.7
1964	219.7	[1] 108.8	201.9
1965	182.9	[1] 110.9	164.9
1966	199.5	[1] 113.9	175.1
1967	215.4	[1] 117.6	183.2
1968	219.1	[1] 122.3	179.1
1969	227.4	[1] 128.2	177.3
1970	234.8	[1] 135.2	173.6
1971	200.0	[1] 141.4	141.4
1972	197.9	[1] 146.1	135.4
1973	207.5	[1] 154.6	134.2
1974	215.6	[1] 169.5	127.2
1975	224.5	[1] 185.8	120.8
Fiscal year:			
1976	[2] 226.2	[3] 197.3	114.6
1977	[2] 262.6	[3] 208.5	125.9
1978	[2] 261.2	[3] 222.9	117.2
1979	[2] 258.2	[3] 241.2	107.0
1980	[2] 277.7	[3] 262.6	105.8
1981	[2] 315.7	[3] 286.5	110.2
1982	[2] 365.3	[3] 309.1	118.2
1983 estimated	[2] 351.3	[3] 333.0	105.5

[1] Implicit price deflator (1958=100), U.S. Department of Commerce, Survey of Current Business, October 1974, November 1978.
[2] Budget authority for liner operators.
[3] Deflator for fiscal years 1978-83 are based on forecast from "Review of the U.S. Economy," Data Resources, Inc., February 1982.

Sources: 1954-1960—MarAd Annual Report, 1973; 1961-1974—MarAd Annual Report, 1975; 1975-1976—MarAd, Office of Financial Management; 1977-1983—MarAd.

Exhibit 2

Foreign Vessel Construction for Subsidized Operators Proposed Amendment to S. 2336

Section 615 of the Merchant Marine Act, 1936 (46 U.S.C. 1101 et. seq.) is amended to read as follows:

> "Sec. 615. The Secretary of Transportation may, until September 30, 1983, authorize an operator receiving or applying for operating-differential subsidy under this Title to acquire, construct or reconstruct its vessels, of over 5,000 DWT and engaged in the foreign trade of the United States, outside the United States if the Secretary finds and certifies in writing that there are inadequate construction differential funds available to meet the operator's construction or reconstruction requirements.
>
> Any vessel acquired, constructed or reconstructed in accordance with this Section or § 1610 of P.L. 97-35 and any liner vessel heretofore acquired, constructed or reconstructed and under charter to the Military Sealift Command on June 1, 1981, shall when documented under the laws of the United States, be deemed for purposes of all laws of the United States to have been constructed or reconstructed in the United States, except that it may not, unless it would otherwise be lawful, engage in the coastwise or domestic trade on any voyage other than those voyages specified in the first sentence of Section 506 of this Act. Such vessels shall, when operated in the domestic trades enumerated in the first sentence of Section 506, pay to the Secretary an amount equivalent to the CDS abatement therein specified, substituting 50 percent of the cost of an equivalent vessel built in the United States without CDS for CDS. This cost estimate shall be made by the Secretary and shall not be subject to appeal. The cost of the equivalent vessel may be approximated to within 3 percent, and shall include interest charges as specified in Federal Register Vol. 45, No. 201, page 68393; 46 CFR Part 276.

Exhibit 3

United States Lines, Inc. (U.S. Lines) is the only ocean carrier which operates an intercoastal-Hawaiian service as part of its Pacific service within the parameters of Section 506 of the Merchant Marine Act of 1936. Section 506 permits U.S. built vessels receiving construction differential subsidy (CDS) to serve these domestic points in connection with an East Coast-Pacific service, on condition that an amount CDS proportionate to the revenues from the domestic portion of the trade is paid back. If "Build Foreign" legislation does not contain language to permit foreign built vessels to serve this trade in the same manner that vessels receiving CDS serve it under section 506, U.S. Lines would either be prevented from making use of the Build Foreign provision to equip its Pacific service, or would be forced to abandon this trade route, the most important service in its business. Either way, U.S. Lines would be uniquely and severely disadvantaged if legislative language does not take cognizance of this problem.

U.S. Lines operates its Pacific service between the East Coast and the Far East by way of the Panama Canal with eleven line-haul containerships serving the ports of New York, Norfolk, Baltimore, Savannah, Panama, Long Beach, Oakland, Honolulu, Guam, Kaohsiung, Hong Kong, Kobe, Yokohama, Pusan, and with connecting service to Shampo. Hawaii and Guam are served only in the outbound direction from the West Coast. With regard to the intercoastal service and the East Coast/West Coast to Hawaii service, U.S. Lines has been serving these trade routes for approximately 50 years. U.S. Lines' share of the West Coast to Hawaii trade is only 10 percent of the total trade involving participating ocean carriers but is an essential component to the success of its service to the Far East.

The vessels dedicated to the Pacific service were all built in American shipyards with the aid of CDS. Under section 506, such vessels must be operated exclusively in foreign trade "or a round voyage from the Atlantic Coast of the United States to the Orient which includes intercoastal ports of the United States, or on a voyage in foreign trade on which the vessel may stop at the State of Hawaii . . ." As stated, U.S. Lines has, for a very long time, been serving the intercoastal and Hawaiian trades under the authority of Section 506 and has been paying back part of its CDS to MarAd under the revenue payback formula.

If the bill does not contain language permitting foreign built vessels to call intercoastally or at Hawaii under the first sentence of section 506, all of U.S. Lines' American competitors in foreign trade would still be able to build foreign as a substitute for building in America with CDS and continue current operations. None of them utilize the first sentence of section 506 by making domestic calls as part of their foreign voyages. For them, such a bill solves the dilemma caused by the end of the CDS program and allows them to stay in business and rebuild or expand their fleets.

As indicated, U.S. Lines is not so protected. It finds itself, without Section 506 language, between a rock and a hard place. It can no longer build American, nor can it build foreign without giving up a trade it has built and nurtured for approximately 50 years.

U.S. Lines recognizes that to allow foreign built or reconstructed vessels to call within the confines of section 506 would be a technical incursion into the Jones Act limitation against foreign built vessels in domestic trades. It must be emphasized, however, that (1) U.S. Lines has been in this trade for almost 50 years; (2) the change is necessitated by the depletion of CDS funds; (3) the domestic calls are severely limited under the first sentence of section 506 to service routes which are predominantly foreign; and (4) there will be a payback similar to the payback now provided for under Section 506.

U.S. Lines requests that the "Build Foreign" amendment allow it to continue serving the trades it has been serving under section 506 with the requisite payback and further restricting such calls to those operators who performed a section 506 service at the time of enactment of this amendment.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR INOUYE AND THE ANSWERS THERETO

Question 1. Is it your understanding that nothing in S. 2366 would permit U.S. ships which are built foreign to carry cargo between Hawaii and the mainland as part of a foreign voyage?

In other words, the Jones Act exception in Section 506 of the Merchant Marine Act of 1936, would not apply to U.S. flag ships built foreign under the provisions of S. 2336?

Answer. S. 2336, as currently drafted, does not permit foreign built or reconstructed U.S. flag ships to carry cargo between Hawaii and the mainland as part of a foreign voyage. It does not currently contain an exception which would permit foreign built or reconstructed vessels under U.S. flag to serve the intercoastal and Hawaiian trade as part of a foreign trade, similar to the Sec. 506 exception permitting CDS built vessels to serve intercoastally and Hawaii as part of a foreign trade.

Question 2. CASO has suggested that an amendment be added to the fiscal year 1983 Authorization Bill which would allow foreign constructed or reconstructed liner vessles to participate in the domestic trade between Hawaii and the mainland as part of a foreign voyage provided that the foreign vessel operator pay to the Secretary of Transportation a pro-rata portion of the foreign/U.S. cost differential. This payment, theoretically, will create cost parity between foreign built and U.S. built ships.

In addition to further eroding of the Jones Act, wouldn't the CASO proposed amendment operate to the disadvantage of the operator of domestic vessels because the cost differential premium does not take into account the payment of interest calculated on the entire unamortized foreign/U.S. cost differential attributable to the domestic portion of the voyage? At today's vessel costs and high interest rates, interest is a substantial cost factor.

Answer. CASO's draft does provide for interest payments. Calculation of interest charges under the CASO amendment refers to the methodology under part 276.3(c), 46 C.F.R., which is the provision for total repayment of the unamortized portion of CDS when the Maritime Administration permits a CDS vessel to be irrevocably brought back to serve only the U.S. domestic trades. Part 276.3(c) does not seem to fit squarely with the partial payback situation dealt with in the amendment.

It must be emphasized that no interest is applicable under current law to partial CDS paybacks when CDS built vessels are partially used in intercoastal or Hawaiian trades under Sec. 506. The CASO amendment attempts to provide U.S. steamship operators with the flexibility to build foreign now that CDS is terminated, under the same operating conditions as it has with CDS. The provision for interest in fact goes well beyond this parity with CDS vessels.

It is difficult to see why an interest should be included in the build foreign provision at all. With CDS, the operator gets the benefit of CDS payments which, when partially paid back under Sec. 506, were considered in the nature of loans. Still, the law does not require interest on this form of payback. With the build foreign situation, the operator is getting no such loan. He is presumably getting the benefit of a lower price, which price must still be financed. Further, under CASO's amendment, he would be paying back a phantom CDS which, in fact, he never receives. To add interest to this phantom CDS is to significantly and, perhaps, prohibitively reduce any benefit to building or reconstructing foreign without CDS.

If compromise is necessary on the interest issue, the calculation of interest must be fair and not prohibitively expensive. Interest should be payable only on the amount paid back for the individual year of payback. For example, assume reconstruction of a vessel costs $10 million foreign and $20 million U.S., and the vessel has a remaining life of ten years after reconstruction. The phantom CDS is $10 million. Assume the vessel is used 20 percent West Coast-Hawaii. The phantom CDS in any one year would be 1/10 of $10 million × 20 percent, or $200,000. Interest would be calculated on the $200,000. If interest were at 12 percent, the payback would be $224,000.

It should be pointed out that to further minimize any impact on the Jones Act, U.S. Lines is willing, as can be seen from earlier submissions, to limit the Sec. 506 exception to reconstruction of existing vessels that are built in the U.S. provided that the operator has historically offered liner service in the 506 trades.

Question 3. Your testimony that "The U.S. shipbuilding industry is relatively healthy and has bright prospects", appears to conflict with the testimony of the Shipbuilders Council of America that its industry is in pretty bad shape. (a) Do the subsidized operators and the shipbuilders differ on this issue?

Answer. The statement of the Shipbuilders Council of America emphasizes the reduction in commercial ship construction recently experienced. That is a matter of fact with which we take no exception. We agree wholeheartedly that it is an unfortunate matter of fact.

As we noted in our prepared statement, the members of CASO have constructed the vast majority of vessels built in U.S. shipyards for the foreign trade since World War II. We would prefer to continue such construction, but can only do so if full parity with our foreign competition is granted. Full parity has not been available for a number of years, and now the CDS program appears dead.

As noted in the enclosed paper, "Subsidized Vessel Operators Should Be Permitted to Acquire, Construct and Reconstruct Ships Abroad When Funds for Government Subsidies To Shipyards Are Not Available", the amount of CDS based U.S. shipbuilding and repair has been very small as compared to Naval shipbuilding and repair, offshore equipment, etc. it is unfortunate that this small percentage of U.S. shipyard work will now be reduced but, in terms of overall shipyard utilization, should not be expected to have a significant impact. The attached paper further explains this and we would ask that it be made a part of your record.

SUBSIDIZED VESSEL OPERATORS SHOULD BE PERMITTED TO ACQUIRE, CONSTRUCT, AND RECONSTRUCT SHIPS ABROAD WHEN FUNDS FOR GOVERNMENT SUBSIDIES TO SHIPYARDS ARE NOT AVAILABLE

THIS PAPER IS A BRIEF SUMMARY OF THE FACTS, EQUITIES, AND NATIONAL IMPLICATIONS INVOLVED IN THIS VITAL ISSUE

Since World War II U.S. shipowners receiving operating assistance from the government have been required to construct and reconstruct their ships in the United States.

Because U.S. built ships cost two to three times as much as ships built in the world market, the government has paid shipyard subsidies (CDS) to ensure U.S. operators rough parity in capital costs.

The Reagan Administration announced that it will virtually eliminate shipyard subsidy through fiscal year 1987.

This action raises a vital national issue: If CDS funds are unavailable and subsidized carriers cannot build abroad they will not be able to build or convert at all and the U.S. liner fleet, already perilously small, will decline further.

As the following pages document, the U.S. shipbuilding industry is relatively healthy and has bright prospects. Conversely, the U.S. liner fleet has declined from 645 ships in 1968 to 233 ships at the first of this year. The number of liner companies has declined from 19 in 1970 to 9 today.

Permitting some foreign construction and reconstruction when shipyard subsidies are not available will permit the survival of the liner fleet without any major impact on shipyards. Many safeguards are built into the proposed amendment:

The Secretary of Transportation must certify that shipyard subsidy funds are not available before any foreign construction activity is permitted.

The amendment applies only to vessels over 5,000 DWT engaged in the foreign trade of the U.S.

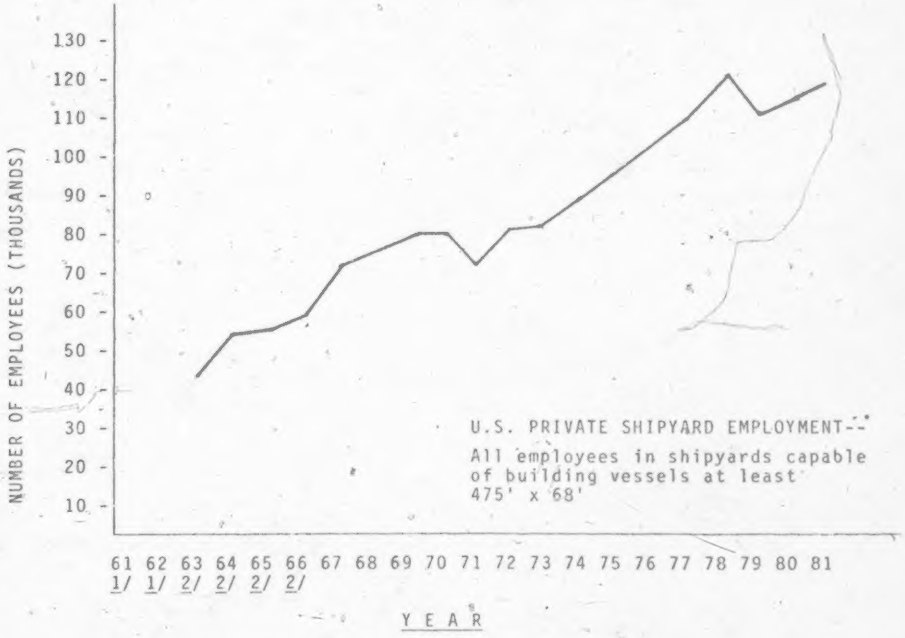
The authority does not affect small boats, barges or tugs, drilling rig vessels or Jones Act ships for the domestic trades.

It is clear that notwithstanding this Committee's action, the Congress will approve the Administration's proposed elimination of new CDS funds for fiscal year 1983.

No shipyard subsidy was requested for fiscal year 1983, and it is the stated intent of the Administration to make only $100 million available per year for shipyard subsidies from fiscal year 1984 through fiscal year 1987.[1]

U.S. liner operators receiving CDS are obligated to contract for new construction to replace up to 58 vessels during this period.[2] Assuming a conservative figure of $100 million per vessel and a shipyard subsidy rate of 50 percent, almost $3 billion would be required. It is clear that these vessels will not be replaced on a one for one basis because new ships are considered more efficient. However, the amount of CDS funds required during this period will be enormous, particularly when the need for conversions, retrofits and repairs are also included.

During the past 21 years, the U.S. shipbuilding industry has experienced substantial growth.



Source: Department of Labor—Bureau of Labor Statistics/Department of Management and Budget.

[1] No figures available.

[2] Production Workers only.

The value of the backlog of 91 Navy vessels on order at the close of 1980 was estimated at $9.0 billion and deliveries will extend through 1987. Eleven shipyards

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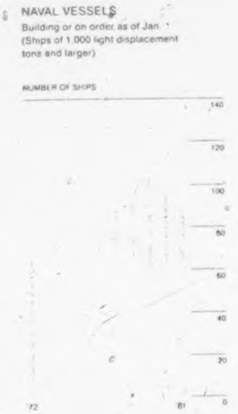
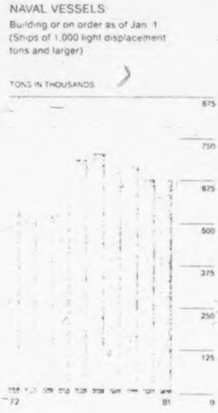
[1] "Major Themes and Additional Budget Details," February 1982, Executive Office of the President, Office of Management and Budget.

[2] U.S. Department of Transportation—Maritime Administration.

(compared to ten at the end of 1979) hold these contracts, one of which is also building four U.S. Coast Guard cutters.





Source: Shipbuilders Council of America 1980 Annual Report.

U.S. shipyards had 72 offshore drilling rigs on order at the end of 1980 with 11 U.S. builders (compared to six at the end of 1979), contracts for 53 were placed in 1980. Valued at about $2.4 billion, deliveries extend into 1984. Worldwide, competition for jackup and semisubmersible rigs intensified during the year as offshore oil and gas fields expanded. In like manner, the demand for new offshore petroleum service vessels has expanded; more than 200 of these supply boats were reportedly delivered in 1980, and an equal number, valued at $2 million each, were on order at yearend.

Also on the plus side of the shipyard ledger, the demand for inland waterway barges as well as for commercial ship repairing services has been strong throughout the year. The dollar value of ship repair work for 1980, both naval and commercial, was estimated at nearly $2,5 billion.

The total value of work in U.S. yards has increased by 86 percent in the 8 years from 1974 to 1981.

SHIPBUILDING AND REPAIR TRENDS AND PROJECTIONS 1974–81

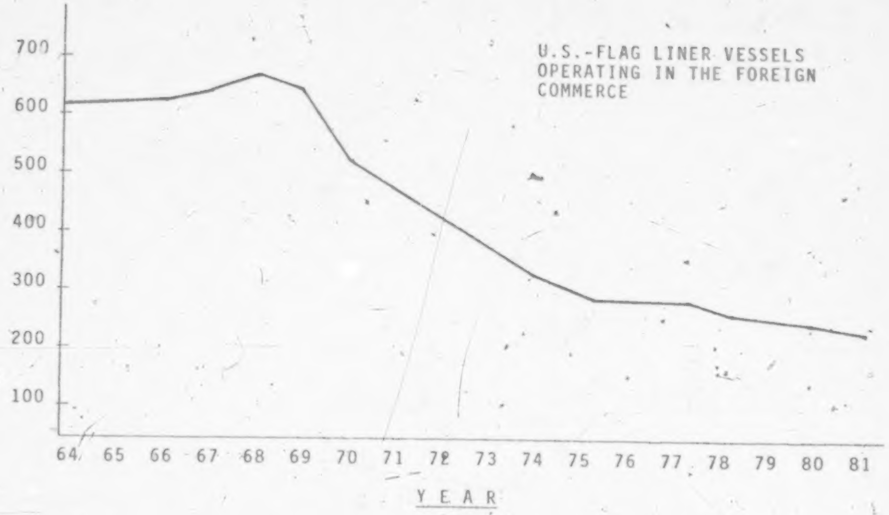
[In millions of dollars except as noted]

ITEM	1974	1975	1976	1977	[1] 1978	[1] 1979	[1] 1980	[1] 1981
Industry [2]								
Value of work done	4,825	5,615	5,896	6,495	6,909	7,549	8,105	8,597
Total employment (thousands)	162.2	166.9	166.3	176.4	172.0	171.6	169.4	166.4
Production workers (thousands)	129.0	133.4	132.1	139.9	136.7	136.4	134.7	132.3
Value added	2,547	2,923	3,287	3,825	3,848	4,205	4,514	4,789

[1] Estimated by Maritime Administration and Shipbuilders Council of America.
[2] Includes value of all products and services sold by the shipbuilding and repair industry.

Source: Bureau of Census, Bureau of Labor Statistics, Maritime Administration, Shipbuilders Council of America.

In the last 16 years, the number of U.S.-flag liner operators has declined from 19 to 9. In this same period, there has been a generally steady (and, from a national security standpoint, *perilous*) decline in the number of U.S.-flag liner vessels operating under the U.S. flag.



Source: U.S. Department of Transportation—Maritime Administration.

Thus, unless this amendment is adopted, it is clear that the liner fleet recognized by the President and military planners as currently inadequate for our national security will continue to decline.

The question, then, really is whether our liner operators will be permitted to build at all, not whether they will build here or abroad.

Certainly a number of marginal shipyards may be facing problems. These are, however, as has been shown, minimal as compared to those faced by our liner industry. It should also be noted that the Office of Management and Budget has estimated that less then 5 percent of those employed in the active shipbuilding base were working on projects including CDS.[1] The shipbuilding base will not only survive should this amendment be adopted but, with increased naval ship construction, naval and merchant ship repair, and construction of other vessels such as supply boats, methanol barges, drill rigs, etc., it should continue its historical growth and profitability.

Question 4. Do you believe that our present cargo preference laws are adequate to ensure that 50 percent of government impelled cargo moves on U.S. flags? Have you had any difficulty getting Agencies to observe the 50/50 requirement?

Answer. At the outset, we note that Chairman Gorton has indicated that your Committee will hold oversight hearings on the cargo preference laws during May of this year. We applaud that and look forward to testifying in detail then. Our answer now will therefore be fairly brief.

We would like to compliment the recent support you, Chairman Gorton, and others gave to those laws during floor debate on S. 1196.

While we have generally felt that our present cargo preference laws are adequate to ensure that 50 percent of government impelled cargo moves on U.S. flag vessels, there have been problems with the enforcement of those laws.

During deliberation in 1980 in the House on H.R. 6899, the proposed Omnibus Maritime Regulatory Reform, Revitalization and Reorganization Act, a CASO supported amendment was proposed. (Copy enclosed.)

This amendment to Sec. 901(b) was intended to modernize the original 1954 statute to reflect the evolution of federal programs since that time. In 1954 when Sec. 901(b) became law (P.L. 83-664), both Senate Report No. 1584 and House Report No. 80 stated that its coverage "... plugs existing loopholes ..." and encompasses "... programs financed in any way by federal funds". Public Law 83-664 was also intended to eliminate procurement and contracting procedures "... by which a high percentage of exports from this country and offshore purchases contracted for, financed, or furnished by the United States, have been routed in foreign vessels in violation of the spirit if not the letter of existing cargo preference legislation".

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[1] Source "Major Themes and Additional Budget Details," February 1982; Executive Office of the President, Office of Management and Budget.

At the time it was enacted, P.L. 83-664 did encompass all the federal programs which generated cargo. However, forms of federal aid programs have continued to evolve while the statute has remained unchanged. In addition, some federal agencies have found devices by which they could circumvent the application of P.L. 83-644 to their programs. As early as 1962, the Senate's Committee on Commerce in it's report (No. 2286) on "Implementation of the Cargo Preference Laws by the Administrative Departments and Agencies" found that "All too often . . . at least several of the administrative departments (have attempted) . . . to evade the cargo preference whenever the opportunity offered". More recently, question has arisen whether the provisions of Sec. 901(b) apply to government grant programs (e.g. the Urban Mass Transportation Administration Act of 1964 authorizing the Urban Mass Transportation Administration of the Department of Transportation to provide financial assistance to several state and local transit bodies for the purchase of urban transit equipment), subcontractors of Department of Defense prime contractors and government cash transfer to foreign nations programs (e.g. AID grants to Israel and Egypt for the unrestricted purchase of items). Ocean cargoes generated by such funds and programs are properly subject to the cargo preference requirements of Sec. 901(b).

The House Report on the bill explained that this provision was "designed to make clear the definition of 'government impelled' cargo". (H. Rep. No. 96-935 Part 1, 96th Cong., 2d Sess. 65 (1980)). The Administration opposed this provision in a June 5, 1980 letter to the Chairman of the House Merchant Marine and Fisheries Committee from the Assistant Secretary of Commerce for Maritime Affairs. That letter added, however, that: "the Administration is committed to avoiding or mitigating adverse effects on U.S. flag carriers in cases where U.S. aid to a foreign government is converted from a Commodity Import Program to cash transfer financing. Where such a change adversely affects U.S. flag carriers, the Executive Branch will take steps to negotiate such changes in the programs as may be necessary to remedy the situation, with due consideration to other U.S. policy objectives. The Administration has already negotiated an agreement in the one such present program to increase the amount of exported grain carried on U.S. flag bulk carriers."

CASO still believes such an amendment may be necessary to modernize Sec. 901(b) sufficiently to accomplish the intent of the original law—to cover all federal programs generating cargo.

We would be pleased to discuss this further at your upcoming hearings.

ATTACHMENT TO ANSWER 4

From H.R. 6899 Mar. 28, 1980 (Key: additions in italic; deletions in black brackets)

SEC. [307.] *306.* Amendments to Title IX.

Title IX of the Merchant Marine Act, 1936 (46 U.S.C. 1241 et seq.) is amended as follows:

(1) Section 901 is amended—

(A) by amending the first sentence of paragraph (1) of subsection (b) to the first colon to read as follows: "Whenever the United States shall procure, contract for, or otherwise obtain for its own account, or shall furnish to or for the account of any foreign nation *or agency* without provision for reimbursement, any equipment, materials, or commodities, within or without the United States, or shall advance funds or credits or guarantee the convertibility of foreign currencies in connection with the furnishing of such equipment, materials, or commodities, *or provide any form of grant, advance, credit, cash transfer, or guarantee whatsoever, to any party,* the approppriate agency or agencies shall take such steps as may be necessary and practicable to assure that at least 50 percent of the gross tonnage of such equipment, materials, or commodities (computed separately for dry bulk carriers, dry cargo [liners] *vessels,* and tankers), which may be transported on ocean vessels shall be transported on privately owned United States flag commercial vessels, to the extent such vessels are available at fair and reasonable rates for United States flag commercial vessels in such a manner as will insure a fair and reasonable participation of United States flag commercial vessels in such cargoes by geographical areas";

* * * * * * *

and

(C) by amending paragraph (2) of subsection (b) to read as follows:

[(2) Every department or agency having responsibility under this subsection shall administer its programs with respect to this subsection under regulations issued by the Secretary of Commerce. The Secretary of Commerce shall review such administration and shall annually report to the Congress with respect thereto.]

"(2) This subsection shall be construed and implemented by each department or agency pursuant to an affirmative plan of action so that its stated purposes and objectives are promptly and consistently achieved. Each department or agency shall develop an affirmative action plan and submit it to the Secretary of Commerce within ninety days of the date of enactment of this subsection. Within ninety days thereafter the Secretary of Commerce shall approve such plan together with such amendments to the plan as he deems necessary or appropriate to further achieve the purposes and objectives of this subsection. Thereafter, no department or agency may alter or deviate from the approved action plan without first consulting the Secretary of Commerce and securing his concurrence. Each plan, as submitted for approval of the Secretary of Commerce and any subsequent amendment thereof, shall be published in the Federal Register for public comment and he shall give due consideration to such comments. Each approved plan shall be published in the Federal Register. Each department or agency shall separately publish in the Federal Register upon approval of its action plan a statement setting forth the name, office address, and duties of each supervisory person having responsibility for the administration of this subsection. Every department or agency having responsibility under this subsection shall administer its program with respect to this subsection under regulations issued by the Secretary of Commerce. The Secretary of Commerce shall review such administration and shall annually report to the Congress with respect thereto."

Senator **GORTON**. The next witness is Mr. Charrier.

STATEMENT OF J. WILLIAM CHARRIER, JR., DIRECTOR, GOVERNMENT RELATIONS, DELTA STEAMSHIP LINES

Mr. **CHARRIER**. Good morning, Mr. Chairman. I am William Charrier, director of government relations for Delta Steamship Lines of New Orleans.

I appreciate the opportunity to appear and present Delta's views on one aspect of the authorization bill presently before the committee.

Delta is a member of the Council of American-Flag Ship Operators, and we fully support the position just delivered by Admiral Holloway. Our comments will be confined to the provision of the bill dealing with foreign construction of U.S.-flag vessels.

S. 2336 as introduced would make permanent the authority of U.S. owners to construct, reconstruct, or acquire vessels abroad, but, as you pointed out, would continue the prohibition enacted last year against the use of the CCF program for foreign-built U.S. flag ships. We believe this prohibition is an inconsistent maritime policy and we would urge the committee to delete it from the bill.

Delta operates a fleet of 24 vessels to South America and West Africa. In all of our trades, the ocean transportation technology is evolving along with the infrastructures of our trading partners. Delta has maintained its competitive position in these trades by introducing the right technology at the right time to meet both shipper demand and the constraints of the ports we serve. This continuing innovation is essential given the extremely strong support extended to national flag lines by the Governments of South America.

We now are in the final stage of negotiating a contract to insert containerized midbodies into six of our multipurpose vessels serving the trade between the U.S. east coast and the west coast of South America. This reconstruction responds to rapidly growing shipper demand for containers in this trade and will, incidentally, give these vessels greatly enhanced national defense value.

Our application for CDS to perform this work in the United States was denied by the Maritime Administration because of lack of funds. It is, therefore, our intention to do this reconstruction abroad.

We view the facts in the current situation as follows:

First, to be a viable long-term investment, the U.S.-flag operator must have cost parity with his foreign flag competition. We charge exactly the same freight rates as our foreign competitors, and, in the long run if any element of our cost structure is significantly higher, we will not achieve the return necessary to justify renewal and expansion of our investment in the fleet.

Second, the Merchant Marine Act of 1936 and subsequent amendments recognized this fact and opted for a cost parity based promotional system rather than for an indirect system based on cargo preference or premium freight rates.

We believe that with the ever increasing importance of international trade to the United States, this conceptual framework for maritime policy is, if anything, more important today than at any time since 1936.

Each of the four essential elements of cost parity, capital costs, operating costs, the tax environment, and financing costs are addressed by one of the elements of the 1936 promotional framework.

Third, the capital construction fund program, especially since its revision in 1970, has proved to be singularly effective in promoting the U.S. fleet. Since that time CCF's have attracted approximately $2 billion in deposits for modernization and expansion.

Disbursements from the CCF's have provided or are providing full or partial funding for $5.2 billion in new U.S.-flag vessel construction. The contractual building obligation which the owner undertakes in exchange for the right to accumulate capital in the CCF is the key to the effectiveness of this program. In our own case, the equity intended to investment in our midbody program is in our CCF.

Fourth, and perhaps most important, under the present conditions and in the absence of CDS, no construction of U.S.-flag ships for the international trades will take place in U.S. shipyards. The elimination of funding for CDS removes the linchpin in the traditional linkage between construction in the United States and the other maritime promotional programs. S. 2336 recognizes this fact.

It makes little sense to us, however, to provide the U.S.-flag operator with the means to achieve capital cost parity in the absence of CDS through foreign construction and at the same time to remove tax cost parity for this foreign construction. This is in essence what the foreign building provision of S. 2336 in its present form would do.

So, the bottom line is this: The prohibition against CCF for foreign built vessels will not help U.S. shipyards. On the other hand, U.S.-flag operators are unnecessarily placed at a cost disadvantage. In our case, for example, a majority of our competition is either government owned or affiliated and pays no tax at all.

This provision reintroduces, as Admiral Holloway pointed out, the tax bias against investing in the U.S.-flag fleet which the CCF program was designed to eliminate in the first place. It would achieve the result, which we find frankly astounding, that a U.S.-owned foreign-built foreign-flag vessel would receive a more favorable tax treatment under subpart F of the revenue code than would a U.S.-flag ship built abroad. Without the CCF program, our ability to accumulate the capital to renew and expand our fleet will be significantly curtailed.

We, therefore, strongly urge the committee to make the CCF program available to all U.S.-flag operators in the international trades regardless of where their vessels are built. We believe that this is an appropriate response to the termination of construction subsidy funding and goes hand in hand with the permission to acquire foreign-built ships.

Thank you.

Senator GORTON. Thank you.

I would like to ask you a series of questions on your own company as illustrative of this problem.

How many vessels does Delta anticipate building or rebuilding during the course of the next 5 years or so?

Mr. CHARRIER. In the course of the next 5 years we anticipate reconstructing six vessels.

Senator GORTON. How much money do you have deposited in CCF accounts?

Mr. CHARRIER. Approximately $80 million.

Senator GORTON. What percent of your annual profits do those deposits represent on a year-by-year basis?

Mr. CHARRIER. I would have to go back through the statements. For the last year that I am familiar with, Senator, I believe that all of the taxable profits of the company were deposited in anticipation of this reconstruction program.

Senator GORTON. What tax penalty would you have to pay if you withdrew those CCF moneys for nonqualified vessel construction out of that $80 million?

Mr. CHARRIER. Well, the entire $80 million would not be needed for the equity portion of this reconstruction.

Senator GORTON. But for purposes of comparing it, if you were to use that whole $80 million for nonqualified construction, what would have to come off the top for taxes?

Mr. CHARRIER. If we withdrew the entire amount, 46 percent of $80 million plus there are some penalties involved in nonqualified withdrawals. In addition to the tax due there are some penalties involved in a nonqualified withdrawal.

Senator GORTON. Is the $80 million which you have now sufficient to provide the equity portion of all of the construction which you intend to accomplish over the next 5 years?

Mr. CHARRIER. Yes, sir, it is adequate. Part of the project will be financed and, of course, there is a very significant investment in containers that goes along with this.

Senator GORTON. Would that answer be true if you were building in the United States as opposed to overseas? What would the difference be?

Mr. CHARRIER. With or without CDS?

Senator GORTON. Without CDS but being able to use your CCF. If you could use it overseas, how much more would you get out of the money?

Mr. CHARRIER. Well, when we originally went into this project, we bid the project to eight U.S. shipyards. Two of them responded with formal bids and the pricing was approximately twice the level of the quotes from the foreign shipyards. This is a reconstruction project which involves not the most complex shipbuilding technologies, but it is a fully containerized midbody. The responses that we got indicated a differential of about two to one.

Senator GORTON. So, under those circumstances and faced with the proposition that under present law if you went overseas you would pay 46 percent in taxation, it would just about be a wash, wouldn't it? The $80 million would go about the same distance in the United States where it would be untaxed as it would overseas if it were taxed. On the other hand, if you were exempted from that taxation you could do twice as much with it overseas. Is that an accurate statement?

Mr. CHARRIER. I believe so, yes.

Senator GORTON. In your written testimony here you state and I quote:

> Each of the four essential elements of cost parity is addressed by one of our maritime promotion programs; capital cost parity by the CDS program, operating cost parity by the ODS program, financing cost parity by the title XI program and tax cost parity by the CCF program. If any one element in the parity equation is missing, the entire system breaks down.

It is true, isn't it, that parity could be achieved by some other alternative means? You don't have to have precisely this combination, do you?

Mr. CHARRIER. Well, if there is a higher cost, there are really only two places it can be borne. It can be borne through higher freight rates which is really impractical. Whatever you might say about the bulk business, in the liner business, it is impractical to achieve that.

Senator GORTON. Let's be more specific. What about the impact of the acceleration cost recovery system in last year's tax bill as long as you are still able to take an investment tax credit?

Mr. CHARRIER. Our opinion is that the CCF program still provides a very important element in combination with ACRS. The reason for that is shipbuilding tends to follow fairly long cycles. We will build new vessels quite infrequently, and the acceleration provided by ACRS can leave you in a position where you will need to bridge a period, depending on what your depreciation picture is, until such time as the market is ready for a new investment in a particular trade.

I think the bottom line, though, is that our competition pays no tax.

Senator GORTON. You mean your foreign competition.

Mr. CHARRIER. Our foreign competition pays no tax.

Senator GORTON. Would it be equitable for us simply to repeal that tax exemption?

Mr. CHARRIER. For whom?

Senator GORTON. For your competition which is operating foreign-flag vessels.

Mr. Charrier. I don't know how we can repeal the tax provisions of another country's laws. You mean their tax position in the United States?

Senator Gorton. Yes.

Mr. Charrier. The problem with that is that would simply inject an element of higher cost across the board into the U.S. trades which would put exporters and importers in the United States at a disadvantage to say Europe or Japan because the facts of life are that out there in the shipping environment there is either no tax or very low tax.

Senator Gorton. Thank you very much, Mr. Charrier. You have presented your case extremely well. We are happy to have had you here.

Mr. Charrier. Thank you, sir.

[The statement follows:]

STATEMENT OF J. WILLIAM CHARRIER, JR., DIRECTOR OF GOVERNMENT RELATIONS, DELTA STEAMSHIP LINES, INC.

Good morning, Mr. Chairman and Members of the Committee. I am William Charrier, Director of Government Relations for Delta Steamship Lines. I appreciate the opportunity to appear here to present Delta's views on one aspect of the fiscal year 1983 Maritime Authorization Bill presently before the Committee.

My statement will be brief. Delta is a member of the Council of American-Flag Ship Operators and we fully support the CASO position on S. 2336 just delivered by Admiral Holloway. Delta's comments will be confined to one provision of the Authorization Bill, that dealing with the foreign construction of U.S. flag vessels. S. 2336 as introduced would make permanent the authority of U.S. flag owners to construct, reconstruct, or acquire vessels abroad without forfeiting eligibility for Operating Differential Subsidy or Government generated preference cargoes. However, the Bill continues the prohibition enacted last year against the use of the Capital Construction Fund program for foreign built U.S. flag ships. We believe this prohibition is poor maritime policy and urge the Committee to delete it from the Bill.

Delta operates a fleet of 24 vessels to South America and West Africa. In all of our trades, the ocean transportation technology is evolving along with the infrastructures of our trading partners. Delta has maintained its competitive position in these trades by introducing the right technology at the right time to meet both shipper demand and the constraints of the ports we serve. Our introduction of LASH vessels connecting the river systems of the U.S. Gulf and the east coast of South America is an example. Such continuing innovation is essential given the extremely strong support extended to national flag lines by the Governments of South America.

Delta is now in the final stage of negotiating a contract to insert containerized midbodies into six of our multi-purpose vessels serving the trade between the United States east coast and the west coast of South America. This reconstruction responds to rapidly growing shipper demand for containers in this trade. The reconstructed vessels will be capable of handling both containerized and break bulk cargo with the vessel's gear, in addition to having extensive refrigerated capacity. This flexibility, demanded by the nature of the trade, will give these ships extraordinary national defense value.

Our application for construction differential subsidy to perform this work in the United States was denied by the Maritime Administration because of lack of funds. It is, therefore, our intent to do this reconstruction abroad.

We view the facts in the current situation as follows:

First, to be a viable long term investment, the U.S. flag operator must have cost parity with his foreign flag competition. We charge the same freight rates as our foreign competitors and in the long run, if any element of our cost structure is significantly higher, we will not achieve a return that justifies the renewal and expansion of our investment in the U.S. flag fleet.

Second, the Merchant Marine Act of 1936 and subsequent amendments recognized this fact and opted for a cost parity based maritime promotional system rather than for an indirect system based on cargo preference and premium freight rates. We believe that with the ever increasing importance of international trade to the United States, this conceptual framework for maritime policy is, if anything, more important today than at any time since 1936. Each of the four essential elements of cost parity is addressed by one of our maritime promotional programs; capital cost parity by the CDS program, operating cost parity, by the ODS program, financing cost parity by the Title XI program, and tax cost parity by the CCF program. If any one element in the parity equation is missing, the entire system breaks down.

Third, the CCF program, especially since its revision in 1970, has proven to be singularly effective in promoting the U.S. flag fleet. Since that time, CCFs have attracted $2 Billion in deposits for modernization and expansion of the U.S. fleet. Disbursements from CCFs have provided or are providing full or partial financing for $5.2 Billion in new U.S. flag vessel construction. The contractual building obligations which the owner undertakes in exchange for the right to accumulate capital in the CCF is the key to the effectiveness of this program. In our own case, the equity intended for investment in our midbody program is in our CCF.

Fourth, in the absence of CDS, no construction of U.S. flag ships for the international trades will take place in U.S. shipyards. The elimination of CDS removes the linchpin in the traditional linkage between construction in the United States and the other maritime promotional programs. S. 2336 recognizes this fact. It makes little sense, however, to provide U.S. flag operators with the means to achieve capital cost parity in the absence of CDS through foreign construction and at the same time to remove tax cost parity for this foreign construction. This in essence is what the foreign building provision of S. 2336 in its present form would do.

So, the bottom line is this: The prohibition against CCF for foreign built vessels will not help U.S. shipyards at all. On the other hand, Delta and other U.S. flag ship operators are unnecessarily placed at a competitive cost disadvantage. In our case, for example, a majority of our competition in the service for which we are reconstructing these vessels is either Government owned or affiliated and pays no tax. This provision re-introduces the tax bias against investing in the U.S. flag fleet which the CCF program was designed to eliminate in the first place. It would achieve the result, which we find frankly astounding, that a foreign built foreign flag vessel owned by a U.S. corporation would receive more favorable tax treatment under Subpart F of the Revenue Code than would a U.S. flag ship built abroad. From Delta's perspective, our ability to accumulate capital to renew and expand our fleet at the end of this decade will be significantly curtailed and the confidence of our directors and stockholders in our Government's determination to have a strong U.S. flag fleet will certainly be diminished.

We, therefore, strongly urge the Committee to make the CCF program available to all U.S. flag operators in the international trades regardless of where their vessels are built. We believe that the legislative language proposed by CASO is an appropriate response at this time.

Thank you.

Senator GORTON. Mr. Hood.

STATEMENT OF EDWIN M. HOOD, PRESIDENT, SHIPBUILDERS COUNCIL OF AMERICA

Mr. HOOD. Good morning, Mr. Chairman.

Senator GORTON. Good morning. You may proceed.

Mr. HOOD. I will be brief.

Before I begin, Mr. Chairman, let me convey to you the heartiest congratulations of our membership on your selection by the Navy League of the United States to receive the Vincent T. Hirsch Maritime Award for outstanding achievement.

Senator GORTON. Thank you, Mr. Hood.

Mr. HOOD. Having said this, I hope you will not think me disrespectful in disagreeing with certain aspects of S. 2336.

Senator GORTON. Not at all. That is why we had you here. So, you just go right ahead.

Mr. HOOD. Most particularly we are concerned by the intended elimination of CDS funding while the study syndrome in the search of alternatives is prolonged by the administration.

As you know, commercial ship construction in the United States is receding precipitously. Of the 11 yards now building merchant vessels, 7 will exhaust their order books by the end of 1982, and the backlog in the remaining 4 yards will then drop to only eight vessels. There has been no improvement in the prospects for additional contracts since I testified before this distinguished subcommittee last year. The situation is indeed even worse.

We also strenuously oppose the provision of S. 2336 which is intended to make permanent the payment of ODS to vessels built or converted in the shipyards of other countries.

With any rational reading of the legislative history surrounding enactment of the Merchant Marine Act of 1936, it can be logically concluded that the availability of ODS was predicated on the construction and/or conversion of original and replacement vessels in American shipyards. The underlying purpose was to insure the maintenance of a commercial shipbuilding capability under sovereign jurisdiction to serve national interests.

Now some foreign shipbuilders are offering to build or convert merchant ships at bargain basement prices. Their governments are a major factor in these below-cost political pricing practices. Foreign governments are indeed indemnifying shipyard losses through an extraordinary array of substantial direct and indirect subsidies while the United States is moving in the opposite direction with respect to the shipbuilding supports.

As I testified last year, the expected expanded naval shipbuilding program does not and will not compose a quick remedy to the elimination of CDS. Because of the long lead time associated with the construction of sophisticated warships, the full impact on shipbuilders of the expanded Navy program is at least 3 years away, and ultimately less than two-thirds of the present production base will be potentially utilized.

Meanwhile at least half of the major U.S. shipyards with the facilities and the skills to produce the larger combatant and auxiliary ships projected in the Navy's five-year plan are now running out of work. New contracts may come too late to avoid further production and employment disruptions.

In January 1979, only 3 years ago, a peacetime peak of 75,000 workers engaged in naval ship construction was reached. Over the past 5 years, annual congressional appropriations averaging 16 new ships per year, have not sustained that same level of employment. At the start of this year employment requirements for naval construction dropped below 60,000, and by the end of this year that figure could be less than 50,000.

One point, Mr. Chairman, must be made perfectly clear and emphasized in the strongest possible language. Under no conceivable circumstances will the planned additions to the naval fleet utilize the full capabilities nor command the full potential of the shipbuilding industrial base, facilities, support activities, and work force as now structured.

The present active shipbuilding industrial base comprises 26 shipyards which have the facilities and work force to construct oceangoing ships and are currently seeking contracts to build them. Of the 26 yards, 8 are now engaged primarily in naval ship construction although 4 of these are maintaining their employment levels with additional commercial work. The workload at the two other yards is about equally divided between Navy and commercial work.

Based on the present 5-year naval shipbuilding plan, it is estimated that by 1985 a maximum of another 4 yards will join the naval shipbuilding fraternity making a total of 14. In other words, the remaining 12 shipyards in the base, as well as a significant share of the yards now involved with Navy work will continue to need merchant ship construction opportunities if the industrial base is to be maintained for future need.

There has also been a serious decline in skilled shipyard workers devoted to merchant ship construction, from a peak at the start of 1976 to less than 10,000 by the end of this year. When coupled with the concurrent decline in naval shipbuilding, this means that some 50,000 skilled shipyard workers and another 77,000 workers in supporting industries have shifted their efforts in the past 7 years from the essential task of building ships.

Facilities for merchant ship construction will be the first to be idled, some perhaps permanently, and many thousands of skilled shipyard workers, including a high percentage of minorities, will be looking for jobs. This diminution of our Nation's shipbuilding industrial base should be a matter of disturbing relevancy to the Congress, as well as to the policymakers in the administration charged with insurance of national security.

Finally, Mr. Chairman, we are opposed to the concept of annual limitations on title XI Federal ship mortgage guarantees as proposed in sections 3 and 4 of S. 2336. You will recall that a very credible case for the extension of this program was made by the committee for title XI vessel financing before hearings of the task force&n Federal credit of the Senate Budget Committee which you conducted in February.

Because of the long-time effectiveness of this program in terms of generating shipbuilding activity, our position is that the statutory title XI ceiling should be raised to $15 billion. We also endorse the testimony of the committee for title XI financing which is to be presented as a part of these hearings. Thank you, Mr. Chairman.

Senator GORTON. Mr. Hood, while I know that this is a very broad question, perhaps you can give me at least an outline of an answer.

One of the principal problems I have as the Senator from the State of Washington is in connection with the production and even the sale overseas of aircraft. The United States is an exceedingly efficient producer of aircraft. In fact, our foreign sales problems are due largely to the fact that less efficient producers overseas end up heavily subsidizing their production.

We have exactly the opposite situation in the industry which you represent.

Mr. HOOD. Correct.

Senator GORTON. The lowest cost differential I have heard anyone testify to here today between the United States and foreign production is 2 to 1. Others said 2½ to 1 and others 3 to 1. What is there fundamentally about the U.S. economy or shipbuilding which causes such tremendous and apparently almost permanent cost differentials? Is there a way for your industry to be competitive in a free market and to be able to produce ships for a price comparable to those of foreign countries?

Mr. Hood. The one word you imply, Mr. Chairman, "volume" applies with respect to the analogy to the aircraft industry. Aircraft from the plants in your State are produced in volume and have been for many years. This is what is needed in the shipbuilding industry to get prices down.

We have been in the 1'sies, 2'sies, and 3'sies business for most of the years that I have been around, and you cannot produce at low cost when you are really tailormaking a vessel.

Senator Gorton. Well, what do we have to do; triple, quadruple, multiply by 10 our projections and subsidize those for an extended period of time in order to create this situation?

Mr. Hood. No; I think if you look at some of the needed sealift requirements that have been put on the public record and before committees of the Congress by military authorities, you will conclude that this country needs a substantial number of merchant-type vessels for national security. How they are to be financed, I cannot tell you. I see no orders coming into our industry at the moment and I doubt that they will be forthcoming in the next year or two, but national security demands are still to be met.

Senator Gorton. You build your statement around the proposition that there has been no comprehensive governmental move to counter the decline in shipbuilding activity and employment. If we look to a little longer time range, however, than your testimony, say back to 1970, haven't we essentially doubled shipyard employment in that period of time and aren't we just still a little bit below the 1980 peaks?

Mr. Hood. Well, I am not sure I agree with the statistics on which your question is based. The 1970 act, yes, sir, was intended to produce a shipbuilding program of 300 ships over a period of 10 years.

Senator Gorton. What was its effect on employment in shipyards?

Mr. Hood. I don't have that number at my fingertips but I will provide it for the record, Mr. Chairman.

I was leading into an answer to your question in terms of a recent timeframe. In terms of the 26 yards in the shipbuilding industrial base, several years ago the peak was 120,000 people. Today it is down to 110,000 people and by the end of this year it will be less than 90,000 people.

[The following information was subsequently received for the record as follows:]

Shipbuilders Council of America,
Washington, D.C., April 26, 1982.

Hon. Slade Gorton,
Chairman, Subcommittee on Merchant Marine, Committee on Commerce, Science and Transportation, U.S. Senate, Washington, D.C.

Dear Mr. Chairman: At the hearing on April 20, 1982 pertaining to S-2336, the proposed fiscal year 1983 Maritime Administration Authorization Bill, I promised to furnish for the record information indicating the effect of enactment of the Merchant Marine Act of 1970 on shipyard employment.

Our statistics, which conforms with those of the Maritime Administration, indicate that total shipyard employment within the active shipbuilding industrial base rose from 92,460 as of January 1, 1970 to 116,419 as of January 1, 1980. This increase of nearly 24,000 workers can be attributed to the impetus of the 1970 Act plus an upswing in naval shipbuilding. However, this calculation is subject to several caveats:

(1) The 1970 Merchant Marine Act envisioned a program of 30 ships per year, for a total of 300 in the 1970 decade, but only 82 were ordered primarily because of the world shipping depression resulting from the 1973 oil embargo, (2) a peak in merchant shipbuilding was reached in 1976 and a peak in naval shipbuilding was reached in 1979, but in both cases, the subsequent employment curve has been steadily downward, and (3) total employment in the shipbuilding base will very likely drop to less than 90,000 workers by the end of 1982 in which eventuality, the level of employment will return to that which existed in 1968.

We stand ready to provide any additional data you may desire.

Sincerely,

EDWIN M. HOOD, *President.*

Senator GORTON. That sounds pretty mild as a downturn in comparison with the auto industry or the steel industry, doesn't it?

Mr. HOOD. Yes, sir, but remember that the total employment in the industry, including all of the many large and small shipyard facilities throughout the country, and there are 600-some, is about 170,000 people, and many shipyards are located in areas of chronic unemployment.

Senator GORTON. Well, I guess that does lead to my next question. As you can see, I am troubled in this area about just what the Federal responsibility is. We are being asked to appropriate something like $20 billion in 1983 for naval construction and $100 billion or so over the next 5 years or so. Given our budgetary constraints, do you really think that there should be appropriations for more aid to shipbuilding even than that?

Mr. HOOD. Looking at the military program, Mr. Chairman, you will find that better than 50 percent of that money will go for expenditures in four shipyards. This would be for aircraft carriers, submarines, and Aegis missile cruisers.

Senator GORTON. Well, I understand that, but it is still a tremendous amount of money.

Mr. HOOD. Yes, sir, it is.

Senator GORTON. What kind of allocation of the limited resources of the United States is appropriate, if that is too low, for shipbuilding?

Mr. HOOD. Well, I don't quite know how to answer your question.

Senator GORTON. How many more millions of dollars?

Mr. HOOD. I could only make a wild guess.

Senator GORTON. OK. How much of the problem in attracting merchant shipbuilding contracts is a labor/management problem in facing competitive realities? Have there been any negotiations in the shipbuilding area remotely comparable to those, say, in automobiles?

Mr. HOOD. The most recent negotiated contract, Mr. Chairman, was with the shipyard in Chester, Pa., which was formerly known as Sun Ship and was acquired several months ago by the Levingston Shipbuilding interests of Orange, Tex. The yard is now called Pennsylvania Shipbuilding Co. The contract, as overwhelming approved by the union, provides for no increase in wages for a period of 1 year and thereafter a very limited increase leading to a profit-sharing or bonus arrangement after 3 years.

Senator GORTON. So it is your view that that is somewhat comparable to the UAW?

Mr. Hood. I find more realism, on the part of shipyard unions, yes, sir.

Senator Gorton. The very last paragraph of your statement deals with credit and credit programs. How do you propose that Federal allocation of credit be controlled, if not by an annual limitation on Federal loan and loan guarantee programs?

Mr. Hood. I believe it has been fairly well controlled thus far, Mr. Chairman.

Senator Gorton. Well, if we take Federal credit programs overall, that just isn't true. Federal credit has gone up faster than the budget has.

Mr. Hood. I thought the point was made very prominently in the hearings before your Budget Committee task force that this program does not distort credit markets and that it has been self-paying and that it has not been a drain on the public Treasury.

Senator Gorton. Nevertheless, it is a Federal allocation of credit, and how do you propose that Congress control the allocation of Federal credit unless it does it annually as a part of the budget process? What alternative do you have?

Mr. Hood. As long as you stay within the ceiling as prescribed by statute aren't you providing control?

Senator Gorton. So we should put a dollar ceiling but not a time ceiling?

Mr. Hood. That is correct. I stand by the testimony of the people who are going to follow me on this subject.

Senator Gorton. But at least you prefer our bill in this respect to the one that the administration sent up?

Mr. Hood. Correct.

Senator Gorton. In the absence of CDS, will any ships, other than Jones Act ships, which can't receive subsidy, be built in U.S. shipyards for international trade?

Mr. Hood. Very unlikely.

Senator Gorton. If that is true, what work will be lost to U.S. shipyards if the CCF program were available for foreign construction?

Mr. Hood. Probably none, except that there are those that believe that CCF rather than being extended to foreign building should be extended to other aspects of U.S. building.

Senator Gorton. Could you expand on that a little?

Mr. Hood. The inland waterways barge construction, offshore platforms, and extension out to the Outer Continental Shelf for any equipment that would go there.

Senator Gorton. My last question to you is a sort of how would you like your poison, but I am going to try it on you anyway.

S. 2336 as introduced makes permanent the authority of U.S.-flag subsidized operators to build their vessels abroad. It does continue the prohibition which was enacted last year against the use of the CCF program for such vessels. CASO, from whom you have just heard here, has suggested alternative language which will allow CCF to be applied to foreign-built vessels but would only extend the building authority to September 30, 1983. Which of those two is less bad as far as you are concerned?

Mr. Hood. They would extend the building authority?

Senator Gorton. Yes; they would allow use of their CCF, but would terminate the authority in 1983. Is that better than the proposal in the bill which still prohibits them from using CCF but makes the policy permanent?

Mr. Hood. The 1983 expiration date is already a matter of law, correct?

Senator Gorton. No; it is 1982 now. It is this year now in the present law.

Mr. Hood. I thought it was extended until September 30, 1983.

Senator Gorton. Well, whatever. Would you rather have——

Mr. Hood. Foreign building or CCF?

Senator Gorton. Yes; which of those two? Would you be willing to allow them to use their CCF funds overseas if you were pretty sure the whole thing was going to be over in 1½ years from right now, or would you prefer the form of this bill, which cuts them off from the use of CCF overseas but makes permanent their authority to build vessels abroad?

Mr. Hood. With respect to CCF I would prefer the form or language of your bill.

Senator Gorton. Well, it is a "which poison would you prefer" question and you aren't going to answer it.

Senator Gorton. Senator Kasten.

Senator Kasten. I have no questions.

Senator Gorton. Thank you very much. We have two more witnesses.

[The statement follows:]

STATEMENT OF EDWIN M. HOOD, PRESIDENT, SHIPBUILDERS COUNCIL OF AMERICA

Mr. Chairman, members of the subcommittee: I am Edwin M. Hood, President of the Shipbuilders Council of America, a national industry trade association composed of major shipbuilders, shiprepairers and ship component manufacturers (see Attachment A) which has now been in existence for 61 years. Our purpose is, and has always been, to enhance the construction and repair of merchant and naval vessels in American shipyards by American workers with American products.

Before I begin, Mr. Chairman, let me convey to you the heartiest congratulations of our membership on your selection by The Navy League of the United States to receive the Vincent T. Hirsch Maritime Award for Outstanding Achievement. The citation of this coveted award refers to your "forceful and active leadership in bringing about a general consensus among the executive and legislative branches of the government and the maritime community about what must be done now to revitalize the Nation's merchant fleet." To quote a philosopher of ancient times, "reason and judgment are the qualities of a leader," and, in these respects, the people of the great State of Washington, and those of us in Washington, DC who look to "reason and judgment" as a fundamental basis for legislative action can be thankful for your presence in the United States Senate.

Having said this, I hope you will not think me disrespectful in disagreeing with certain aspects of S. 2336, the proposed fiscal year 1983 Maritime Administration authorization bill, your distinguished Subcommittee is considering this morning.

Most particularly, we are concerned by the intended elimination of construction-differential subsidy (CDS) funding while the study syndrome in the search of alternatives is prolonged by the administration.

As you know, commercial ship construction in the United States is receding precipitously. Of the 11 yards now building merchant vessels, seven will exhaust their orderbooks by the end of 1982, and the backlog in the remaining four yards will then drop to only eight vessels. There has been no improvement in the prospects for additional contracts since I testified before this distinguished Subcommittee last year. The situation is indeed worse.

The distinguished writer, John G. Hubbell, in Reader's Digest magazine last month, very cogently diagnosed the U.S. merchant marine as being "in an advanced state of decay." If the Congress and the administration don't soon agree and soon take appropriate action, decay could become deadly. In another respect, only last week, the Secretary of the Treasury observed that the Nation's economy is "dead in the water." The same characterization could be applied to commercial shipbuilding in the United States. But, there has been no comprehensive governmental move to counter the decline in shipbuilding activity and employment.

The Congress has yet to signal this Nation's resolve (1) to the balance of the world that a domestic merchant shipbuilding capability will be adequately maintained, (2) to the shipyard workers of America that they are essential to the maintenance of that capability, and (3) to U.S. commercial shipbuilders that their recent substantial investments in capital improvements and techniques will not have been wasted. In the present posture of things, with the elimination of CDS, the signal is very much the opposite: the tone is very much negative.

In this same context, we strenuously oppose that provision of S. 2336 which is intended to make permanent the payment of operating-differential subsidies (ODS) to vessels built or converted in the shipyards of other countries. With any rational reading of the legislative history surrounding enactment of the Merchant Marine Act of 1936, it can be logically concluded that the availability of ODS was predicated on the construction (and/or conversion) of original and replacement vessels in American shipyards. The underlying purpose was to ensure the maintenance of a commercial shipbuilding capability under sovereign jurisdiction to serve national interests.

Now, some foreign shipbuilders are offering to build or convert merchant ships at "bargain basement" prices. Their governments are a major party to these below-cost "political pricing" practices. Foreign governments are indeed indemnifying shipyard losses through an extraordinary array of substantial direct and indirect subsidies, while the United States is moving in the opposite direction with respect to shipbuilding supports.

Understandably, U.S. shipowners want to optimize their capital costs. They want to take advantage of these "bargain basement" prices. They want to be separated from the ODS/CDS connection. Their primary obligations are to their shareholders. Maintenance of a shipbuilding industrial base for national security is but a secondary consideration.

The moralistic conflict between opportunism and established public policy thus becomes more acute. Moreover, the stand of the adminstration in encouraging the award of contracts to foreign shipyards undermines preservation of the recognized domestic shipbuilding industrial base considered essential for national security. That base is today not being maintained, and with the formulation of maritime policy in a state of limbo, the Congress must act immediately and positively, not inconstantly and negatively, to resolve this moralsitic conflict. And, resolution should be directed toward strengthening not imparing the shipbuilding industiral base.

As I testified last year, the expected expanded naval shipbuilding program does not, and will not, compose a quick remedy to the elimination of CDS. Because of the long lead-time associated with the construction of sophisticated warships, the full impact on shipbuilders of the expanded Navy program is at least 3 years away, and ultimately less then two-thirds of the present production base will be potentially utilized. Getting from here to there will not be without hindrance, At least half of the major U.S. shipyards with the facilities and skills to produce the larger combatant and auxiliary ships projected in the Navy's 5-year plan are now running out of work. New contracts may come too late to avoid further production and employment disruptions.

In January 1979, only three years ago, a peacetime peak of 75,000 workers engaged in naval ship construction was reached. Over the past five years, annual Congressional appropriations, averaging 16 new ships per year, have not sustained that same level of employment. At the start of this year, employment requirements for naval construction dropped below 60,000, and by the end of this year that figure could be less then 50,000.

One point must be made perfectly clear and emphasized in the strongest possible language. Under no conceivable circumstances will the planned additions to the naval fleet utilize the full capabilities nor command the full potential of the shipbuilding industrial base—facilities, support activities and workforce—as now structured.

The present active shipbuilding industrial base comprises 26 shipyards which have the facilities and workforce to construct oceangoing ships and are currently seeking contracts to build them. Of the 26 yards, 8 are now engaged primarily in naval ship construction although four of these are maintaining their employment levels with additional commercial work. The workload at two other yards is about equally dividied between Navy and commercial work.

Based on the present 5-year plan, it is estimated that by 1985, a maximum of another 4 yards will join the naval shipbuilding fraternity, making a total of 14. In other words, the remaining 12 shipyards as well as a significant share of the yards now involved with Navy work will continue to need merchant ship construction opportunities if the indusrial base is to be maintained for future need.

There has also been a serious decline in skilled shipyard workers devoted to a merchant ship construction: from a peak of 35,000 at the start of 1976 to less than 10,000 by the end of this year. When coupled with the concurrent decline in naval shipbuilding, this means that some 50,000 skilled shipyard workers, and another 77,000 workers in supporting industries, have shifted their efforts, in the past seven years, from the essential task of building ships.

Facilities for merchant ship construction will be the first to be idled, some perhaps permanently, and many thousands of skilled shipyard workers, including a high percentage of minorities, will be looking for jobs. This diminution of our Nation's shipbuilding industrial base should be a matter of disturbing relevancy to the Congress as well as to the policymakers charged with ensurance of national security. Not only must the strength of our Nation's seapower be measured in numbers of warships and sealift capacity (i.e., U.S.-flag merchant ships), but also in terms of our ability to build both kinds of ships. In terms of maritime strength, the two are inseparable and complementary. And, national interests require that the two be maintained.

Finally, Mr. Chairman, we are opposed to the concept of annual limitations on Title XI Federal ship mortgage guarantees as proposed in Sections 3 and 4 of S-2336. You will recall that a very credible case for the extension of this program was made by the Committee for Title XI Vessel Financing before hearings of the Task Force on Federal Credit of the Senate Budget Committee which you conducted in February. Because of the longtime effectiveness of this program in terms of generating shipbuilding activity, our position is that the statutory Title XI ceiling should be raised to $15 billion. We also endorse the testimony of the Committee for Title XI financing which is to be presented as a part of these hearings.

Thank you, Mr. Chairman, for this opportunity to present our views. I will try to answer any questions you might have.

[The following information was subsequently received for the record:]

Shipbuilders Council of America,
Washington, D.C., April 26, 1982.

Hon. **Daniel K. Inouye,**
U.S. Senate,
Washington, D.C.

Dear Senator Inouye: As you requested at the conclusion of my April 20, 1982 testimony before the Subcommittee on Merchant Marine of the Committee on Commerce, Science and Transportation, I am pleased to answer the following question for the record in connection with Senate Bill 2336: "It appears that the subsidized operators do not share your assessment of the state of the shipyards. CASO, in its testimony, says that 'the U.S. shipbuilding industry is relatively healthy and has bright prospects.' (A) Do you differ with CASO on this issue?"

Answer. The oft-repeated remark that shipbuilding is one of those industires which has many back-seat drivers would seem to be applicable here. CASO's statement to the effect that "the U.S. shipbuilding industry is relatively healthy and has bright prospects" is wholly fallacious and an attempt to juxtapose statistics and facts to support a pre-conceived position incompatible with national security interests as relating to ship construction capabilities.

Interpretation of Bureau of Labor statistics with respect to shipyard employment can be misleading for the reason that these figures reflect employment in some 600 privately-owned business establishments primarily engaged in the construction of off-shore platforms, fishing vessels, inland waterway barges and floating equipment, tugboats, dredges and yachts as well as commercial and naval ships. My testimony was directed to the 26 shipyards, which, it is agreed by government and industry, compose the active shipbuilding industrial base. These are yards having the facilities and skills to construct or convert oceangoing ships or are currently seeking contracts.

In my statement, I projected the current downward trend of shipyard employment devoted to naval and commercial ship construction, and concluded that some 50,000 skilled shipyard workers have been shifted from the essential task of building ships over the past seven years. Many of these affected workers are minorities, and they are or will be looking for jobs in areas of chronic unemployment.

As to "bright" prospects, the Maritime Administrator, in a recent speech, said the Administration is "unable at this time (to) project a major merchant ship construction program" for U.S. shipbuilders, but he expressed hope that "we can achieve such a goal in the period ahead of us." The duration of the "period ahead," unfortunately, was not defined.

Concerning naval prospects, every Navy official concerned with ship construction matters has warned that the real impact of the new five-year shipbuilding plan is at lesat three years away and that even then less than two-thirds of the Nation's production base will be potentially involved.

Obviously, we differ with CASO on this issue, and we stand ready to provide any additional data you may require.

With best personal regards always, I am

Sincerely,

EDWIN M. HOOD, *President.*

Senator GORTON. Mr. Fellows and those accompanying him.

STATEMENTS OF BEN E. FELLOWS, PRESIDENT, TWIN CITY BARGE, INC., AND PRESIDENT, COMMITTEE FOR TITLE XI VESSEL FINANCING, ACCOMPANIED BY THOMAS MILLS, COUNSEL; AND MICHAEL SCLAR, VICE PRESIDENT AND DIRECTOR, MARITIME GROUP OF TEMPLE, BARKER & SLOANE, INC.

Mr. FELLOWS. Thank you, sir. I am Ben Fellows, president of Twin City Barge, Inc., South St. Paul, Minn. I am here in my capacity as president of the Committee for Title XI Vessel Financing and am accompanied by Mr. Michael Sclar, vice president of Temple, Barker & Sloane, Inc., of Lexington, Mass., and Mr. Thomas Mills, counsel to our committee.

Our oral statement will be relatively brief and will be limited to sections 3 and 4 of S. 2336. We have previously submitted a more comprehensive written statement, together with an economic study prepared by Temple, Barker & Sloane [1] and have submitted separately suggested changes of a technical nature, both of which I ask be included in the record.

Senator GORTON. They will be included in the record in full.

Mr. FELLOWS. Thank you, sir.

Mr. Chairman, as an overall assessment, we appreciate what you appear to be attempting to do in S. 2336.

No. 1, if annual allotments are to be made in title XI commitment authority, they should be made by Congress rather than unilaterally by the executive department.

No. 2, we appreciate your attempt to give the title XI program a boost by increasing the release of the fiscal year 1983 commitment authority from $600 million proposed by the administration to $675 million. However, either figure would cut by more than one-half the level of guarantee authority annually approved during fiscal year 1979 to 1981.

Regrettably, we conclude that a mere increase of $75 million in fiscal year 1983 commitment authority, which incidentally is the cost of one coastal tanker, without raising the statutory ceiling, will send the wrong signal to the market and further inject an element of disruptive uncertainty into the industry. In short, S. 2336 will probably do the very opposite of what you intend.

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[1] The study has been retained in the committee files.

How can this be?

After adjusting all the numbers, there is roughly $1.5 billion of remaining statutory authority against which are pending about $3.5 billion in active projects driven by the marketplace requiring $2.8 billion in guarantees. With a statutory limit of only $1.5 billion remaining, it is inconsequential whether that is apportioned cut by $600 million or $675 million in the next fiscal year. Vessel operators will interpret either figure as the death knell for title XI over the next several years and will either abandon their expansion plans or, where practical, shift them overseas.

The point we wish to stress is that to continue its past history of success the title XI program must be structured on a multiyear basis with a minimum of 3 years expectancy.

To understand this it might be helpful to walk through the decisionmaking process in vessel construction and financing and review the sequential steps in administering title XI commitment authority and bond issuance.

If a company wishes to build a new vessel for a particular market, the final decision to proceed with the construction contract depends heavily upon the availability and cost of financing. The construction period will be from 1 to 3 years, depending upon the size and type of the vessel. Multiship contracts can be longer.

After determining the design of the vessel and negotiating a construction contract with a shipbuilder, the company then submits a comprehensive title XI application to the Maritime Administration. If after intensive review of the vessel's design, vessel employment prospects, owner's competence, financial soundness, et cetera, which typically takes at least 9 months or longer, the application is approved, the Secretary issues a conditional commitment to guarantee the bonds in the future, normally within 1 year.

Precisely when the bonds will be issued depends upon a number of factors, including the length of construction period, the arrangements the vessel owner has made for construction period financing, usually with his bank, and very importantly the interest rates levels in the private credit market. Therefore, the actual issuance of the bonds may occur early in the construction period, or it may be done near delivery using bank financing for interim payments to the yard.

Given these sequential steps in the construction, application/approval and financing process of title XI, it is clear that more than one fiscal year is involved and authorization on a multiyear basis is essential.

As we have shown in our written statement, the issuance of conditional commitments by the Secretary within the statutory limit are restrained by the market for vessels and the timing of the issuance of bonds is restrained by interest rate levels.

Thus any attempt to finetune a presumed impact on credit markets in a given fiscal year by apportioning the amount of commitment authority to be released in that fiscal year will disrupt these market forces and with no increase in the statutory ceiling will have profoundly adverse effects. It is these consequences we wish to call to your attention.

In view of these long leadtimes, we who are involved in title XI financing, vessel operators, builders, suppliers, lenders, and labor forces, will perceive S. 2336 as the end of title XI. They will see that only $675 million in commitment authority will be released in fiscal year 1983 against a pending backlog of $3.5 billion in projects. They are being told that they will not know what will be available thereafter until the Congress acts in each subsequent fiscal year.

This injects an element of such uncertainty as to inhibit going forward with capital expansion programs, regardless of how strong the actual market demand may be for the vessels themselves. Worse yet, when the economy finally does turn around and interest rates come down, a misconceived limit on new commitment authority of $675 million would actually stymie recovery of a depressed shipbuilding industry.

Looking at the past history of title XI, as indicated by the chart appended to this testimony, it is clear that the availability of statutory authorization cannot force the building for which there is no market. But unavailability of authority will choke off new building in excess of an arbitrary ceiling.

This market impact is demonstrated by the issuance in 1974 of $1.26 billion in commitments, while in 1975 it was only $699 million although the available statutory authority was $1.48 billion. Similarly, in 1978, only $430 million in commitments were issued when the available statutory authority was $4.6 billion.

It is simply impossible to look into the future and know precisely what the demand for vessels or what interest rates will be. But recognizing that market forces will restrain the use of title XI financing, it is essential that the statutory authorization be high enough to provide for the variations in market forces without artificially restraining investment in capital equipment.

Significantly, the peak of title XI commitments was not in 1980, when OMB imposed its arbitrary and disruptive ceilings on the program, the peak was in 1974. When the markets slackened the commitments slackened significantly during the intervening years.

Mr. Chairman, since one of the main purposes of the 1981 Economic Recovery Act is to promote private investment in capital equipment, this is not the time to put artificial restraints on a program which is limited to investment in capital equipment and promotes substantial private equity investment in the construction of vessels.

This program has not only not cost the Government 1 penny, it generates tax revenues for the Government and would obviate the need for unemployment payments if allowed to continue functioning. In short, its budget is wholly positive, but if gutted would be negative.

We the users have paid for this program. We have paid for its contribution to national defense in shipbuilding base and auxiliary vessels now available and in use in the Military Sealift Command.

We urge you to consider an amendment to sections 3 and 4 of the bill which would extend the program for a minimum of 3 years and provide adequate commitment authorization under proper congressional controls by limiting the increase to $1 billion per year for 3 years. This amendment would track the efforts in the other Chamber but provide more stringent congressional control over the program.

Title XI takes no funds from any other program. It has a long history of unqualified success and could well serve as a model for other guarantee programs in that it is market oriented and costs the taxpayers nothing. We have yet to encounter any arguments against the merits of title XI.

The case to reduce it rests solely on the perceived defects of other off-budget programs. Reducing title XI as an exercise in overall off-budget reductions 133,000 jobs and $9.1 billion in the economy which would otherwise be self-generating.

In summation, Mr. Chairman, we regret we cannot be more supportive of the committee's bill. Were sections 3 and 4 enacted as presently drafted it would, we fear, lead to further disruption and chaos in shipbuilding, a result we are confident you do not intend.

We urgently recommend that you and your colleagues remove the death threat hanging over title XI, a national asset carefully refined through many Congresses and successive Republican and Democratic administrations over the past 34 years.

We understand S. 2336 is essentially a holding piece of legislation for the Maritime Administration, but the title XI program will not stay on hold without calamitous consequences to the maritime industry and the economy.

I thank you for the opportunity to present my views and invite Mr. Sclar to present a brief review of the program's economic impacts. We would then be pleased to answer any questions.

Senator GORTON. Senator Kasten, unfortunately, had to leave before he could ask his questions.

Mr. FELLOWS. Yes, sir.

[The statement follows:]

STATEMENT OF BEN E. FELLOWS, PRESIDENT, COMMITTEE FOR TITLE XI VESSEL FINANCING

I am Ben E. Fellows, President, Twin City Barge, Inc., South St. Paul, Minnesota. I am here in my capacity as president of the Committee for Title XI Vessel Financing. This committee represents a cross section of the U.S. Maritime industry—operators of deep-sea vessels, inland operators of tugs and barges, offshore operators of drilling, tug/supply vessels and specialty-construction vessels, large shipyards, small shipyards, labor, and the supply industry serving operators and yards. I am accompanied here today by Mr. Thomas Mills, Counsel to the Committee and Mr. Michael Sclar of Temple, Barker & Sloane, Inc. of Lexington, Mass., who will testify as to certain aspects of his firm's analysis of the economic impact of the title XI program. The Temple, Barker & Sloane study is submitted for the record as appendix A. We thank you for the opportunity to testify here today on S. 2336.

Because our Committee is solely concerned with the historically successful vessel financing guarantee program under title XI of the Merchant Marine Act, 1936, I will limit my testimony to sections 3 and 4 of S. 2336. In addition, we will submit separately as appendix B comments of a technical nature on section 5.

Before discussing sections 3 and 4 of S. 2336, it would be useful to review briefly the title XI program, and how we got to the problem of annual limitations. The title XI Vessel Financing Program under which the United States guarantees a major portion of the debt to build a new U.S.-flag commercial vessel, has been the primary mechanism for private, independent shipbuilding in the United States under the Merchant Marine act, 1936. Title XI is not a subsidy. Users of the program sell bonds directly in the private market. Users of the program pay user fees which (1) cover all the expenses of the Maritime Administration in administering the program and (2) provide a surplus fund for payment of defaults. The existence of this fund, in combination with the first preferred ship mortgages given the government in return for its guarantee and requirements for additional security, have kept the title XI program from costing the government anything during its 44-year history while making possible the construction of over 7,000 vessels in U.S. shipyards.

In title XI guaranteed vessel financings, after making the statutory findings of economic feasibility, financial and operating ability, and reaching agreement between the Secretary of Transportation and the vessel owner on the amount of equity investment, preferred mortgages, reserve funds and other security arrangements, the Secretary issues a commitment to guarantee bonds to be issued by the vessel owner. However, the guarantee is not issued until the vessel owner, after taking into account the level of interest rates, issues bonds in the private capital markets at the prevailing market rate. Bond proceeds are used only for capital equipment, and then only for U.S.-origin equipment and materials.

The bonds bear the government guarantee but there is no borrowing by the government in connection with the issue of bonds and the government obligation is contingent only. The statutory authorization for title XI financing does not involve appropriated funds but is rather a revolving guarantee authority.

Since November of 1981, the members of our group have been deeply involved in advocating the continuation and enhancement of the title XI program. We joined together as a result of the imposition of arbitrary annual ceilings on title XI by the Office of Management and Budget. One of the most frustrating aspects of our effort has been our inability to get anyone in the executive branch of the government to look at the merits of this program. What we have found is that it was not for lack of merit that the title XI program has been cut. Indeed, the merits of title XI seemed to have been treated as irrelevant.

During the Carter administration, because of what we understand to have been a desire to put in place a mechanism to control the burgeoning amount of off-budget financing programs, OMB sought from this committee authority for annual limitations on the amount of title XI guarantees which could be issued. That authority was denied. Likewise, the present administration, not as part of any specific maritime program, and before it had time to study the effects of any particular loan guarantee program, requested as a part of its initial budget proposals authority to limit title XI on an annual basis. Again, that authority was denied both by this Committee and by the House Merchant Marine and Fisheries Committee. Nevertheless the Office of Management and Budget arrogated to itself the authority so to limit title XI and set $900 million as a limitation for fiscal year 1981 and $1.05 billion as the limitation for fiscal year 1982.

In the summer of 1981, in part through the efforts of the founding members of our title XI committee, $150 million in authority was shifted from fiscal year 1982 to fiscal year 1981. This was necessary because the imposition, for the first time, and without notice, of annual limitations disrupted the market and imposed a severe hardship both upon the shipowners and the shipyards at which their vessels were being built. The arbitrary cuts in title XI by OMB was a classic case of disruptive governmental interference in the marketplace.

At the time the limitation was imposed, and I want to emphasize this, no economic or budgetary analysis of title XI had been undertaken. The dollar limitation was reached, we understand, by looking at what was projected to be utilized and applying an arbitrary across-the-board cut of title XI together with most other guarantee programs. Thus the initially imposed ceiling already represented a 35-40 percent cut in the program. In November of 1981, the newly imposed limitations were cut further—again, across the board with other programs—by 25 percent. By this time, the fiscal year 1982 ceiling was at $675 million, roughly one-half of what traditionally had been utilized and far less than was needed.

The press release accompanying the last across-the-board cut stated that this cut was possible because financing drilling vessels amount to a "subsidy to the oil companies" and would no longer be financed and because LNG vessels would also not be financed. We strongly suspect that that statement was nothing more than an after-the-fact rationalization of the across-the-board cut because by that time no study or analysis of the title XI program had yet been undertaken. In fact, although applications for title XI in respect of LNG vessels are on file, none of those applications were expected to be processed in fiscal year 1982 or, for that matter, fiscal years 1983, 1984, or 1985, and the previous ceiling did not reflect anyone's opinion that LNG vessels would be processed in the forseeable future. Likewise, the statement that financing drilling rigs could be eliminated because it amounted to a subsidy to the oil companies was also incorrect. First, as we will make clear later in our statement, and as this committee already knows, there is no subsidy in title XI; second the major oil companies do not build drilling vessels with title XI. They have been built by smaller, independent companies and, in a market where shipbuilding is heavily subsidized by foreign countries, title XI makes the critical difference in the decision to build an offshore rig in the United States rather than a foreign country. Even the most superficial analysis by the Office of Management and Budget or the Department of Transportation would have shown that.

At the same time, despite President Reagan's express and unequivocal commitment to a storng merchant marine and enhancement of the cirtical U.S. naval shipyard and sub-supplier base, we are told that these cuts indeed have nothing to do with maritime policy but only economic policy. The economic and budgetary policies justifying cuts in loan guarantee programs in general have no applicability to title XI. If anyone had bothered to look at title XI in terms of the adverse economic effects of Federal credit programs sought to be eliminated, this would have been apparent.

The amount of title XI guarantees which may be outstanding at any time is, and has always been specified in the statute and, until the action by the Office of Management and Budget, had never been limited on an annual basis. In practice, however, there are built-in market limitations. The statute requires that the market for the equipment being financed be carefully valuated in order to find economic feasibility. If the transaction does not meet this market and other stringent tests, no guarantee may be issued irrespective of the statutory level of authorization. Consequently, adjustments in the statutory ceiling have traditionally been made at 2-to-3 year intervals. Depicted in the following table are the dollar amounts of guarantees issued compared with the available statutory authority. This shows the rather steady market and administrative constraints on the issuance of new title XI guarantees.

[In millions of dollars]

	Available authority	Commitments issued	Available authority at end
Fiscal year:			
1971	2,117	273	1,844
1972	1,955	648	1,307
1973	1,387	966	421
1974	2,503	1,266	1,237
1975	1,458	699	759
1976	2,856	806	2,050
Transition quarter	2,077	78	1,999
1977	2,166	988	1,178
1978	4,676	430	4,246
1979	4,327	954	3,373
1980	3,620	1,085	2,535
1981	2,611	1,047	1,564

Apart from these limitations, title XI's extreme sensitivity to interest rate fluctuations further governs the timing of the issuance of long term title XI bonds. Thus, these variables plus the very nature of shipbuilding make it impossible to "force" credit on an unwilling market and also make it nearly impossible to serve a valid demand by programming the release of credit guarantees in finite annual increments.

As noted, the limitations imposed by OMB on title XI have not been crafted for title XI after a review of the merits of the program but are part of an across-the-board cut of all so-called off-budget, Federal credit assistance programs. According to the administration witnesses before the Senate Task Force on Federal Credit, the sum of Federal direct borrowing to finance the budget deficit and indirect borrowing through loan guarantee and other Federal credit assistance programs has burgeoned to the point where it now absorbs some 40 percent of the total U.S. credit market. While that is somewhat misleading, because it is our understanding that the administration does not include consumer credit and some other large sources of credit within the United States—thereby overstating Federal absorption of available U.S. credit—we nevertheless agree with the Administration that some control of Federal-direct and sponsored borrowing is warranted.

As users of bond market credit, we are vitally interested in the availability and costs of credit and the aggregate Federal involvement in the credit market. While it appears to us that the real problem is with the size of direct borrowings by the

Treasury, we agree with Administration representatives as to the need for programmatic controls of Federal credit assistance programs, particularly where there is in fact a direct budgetary impact and direct borrowing by the Treasury to support subsidized interest rates. What we disagree with is what has in fact been done: OMB has merely lumped all Federal credit assitance programs together, no matter how disparate in fuctions, economic result, budgetary impact, et cetera—and cut them across the board. No program-by-program analysis has been undertaken comparing each with the economic and budgetary evils recognized to result from Federal credit programs in general and no rational, systematic methodology has been proposed to deal with the problem. In short, OMB slashed title XI because of problems in other programs.

We believe that it makes no more sense to consider all credit assistance programs en masse than it would to consider all appropriations en masse. Each program differs markedly in the way it operates, the statutory goals sought to be achieved, the criteria for qualification and use of a particular credit program, the method by which the loan or guarantee is issued or funded, the degrees of security required and the cost, direct or indirect, to the Federal Treasury.

The reasons articulated by Treasury Secretary Donald Regan and others for cutting back or eliminating Federal credit assistance programs are these: administrative expense in running the programs which is paid out of the Treasury; direct budgetary outlays for interest rate subsidies where the rate is less than the cost of money to the Treasury; payments of defaults which amount to a deferred subsidy; and "distortion" of the U.S. credit markets by crowding out private borrowers who would otherwise make capital investments.

We suggested to the Senate Task Force on Federal Credit that each individual program should be evaluated against those criteria. We further suggested that, at the same time, the economic impact of each program should be addressed by the legisltive committee having jurisdiction over the program. We believe that such an approach would be consistent with that outlined by the administration's witnesses, Assistant Treasury Secretary Mehle and OMB Assistant Director for Economic Development Kudlow, in their statements before the Senate Federal Credit Task Force on December 10, 1981. Now let us measure the title XI program against Secretary Regan's criteria:

Administrative Costs.—The administrative expenses of title XI are paid for by users of the program. There are charges for the processing of applications ("investigation fees") and an annual guarantee fee of one-half to 1 percent on the outstanding balance of the guaranteed financing. These user charges pay for all administrative expenses, including office space, salaries of government employees, travel and other overhead. Last year, for example, the administrative expenses of the program ran somewhat less than $4 million. User fees (investigation fees and guarantee fees) were approximately $48 million, leaving a surplus last year alone of over $44 million. The fund currently has a surplus of over $250 million, and is projected by the administration to reach $360 million by the end of fiscal year 1983.

DIRECT BUDGET OUTLAYS

(a) *Interest rate subsidies.*—Interest rates for title XI bonds are determined by the market and are in excess of the rates on direct obligations of the Treasury for comparable securities. Users of title XI sell notes or bonds with the government guarantee directly in the private credit market. Title XI operates independently of the Federal Financing Bank and there is no direct borrowing by the Treasury.

(b) *Defaults.*—The Government's obligation with respect to title XI financing is contingent only and drawing against the Treasury could occur only if there are defaults which cannot be covered by the user charges paid into the Ship Financing Fund or realization on the security. In the history of the title XI program to date there has not been a drawing on the Treasury because of a default under title XI. There have been some defaults including some potentially large defaults because of the bankruptcies of Pacific Far East Line and States Steamship Line in the mid-1970's. Nevertheless, because the government has a first preferred ship mortgage on each vessel in respect of which it guarantees the financing and secondly because of the user funded title XI ship financing fund, described above, the government has not had to draw on the Treasury to make good on a default.

Over the history of the program, 11 defaults have occurred with a cumulative default rate of only 0.8 percent of total guarantee commitments extended. On an annual basis, this loss record is extremely low, slightly more than 0.1 percent of outstanding commitments, and compares favorably with the largest commercial banks on their commercial loans which have a much shorter average maturity than title

XI. Thus, sound program management, a diversified portfolio, prime security interest and self generating reserves have resulted in a program that has cost the U.S. taxpayer nothing while assisting in the building of over 7000 vessels.

Distortion of Credit Market.—Title XI also measures well against the last of Secretary Regan's criteria—the distortion of the credit market. Title XI guarantees accounted for only 1.2 percent of the total Federal loan guarantees, direct loans and federally insured loans outstanding in 1981, and that is also the average percentage over the last 6 years. Moreover in fiscal year 1980 title XI accounted for only 1/400th of the total direct Federal or federally sponsored borrowings in U.S. credit markets. Its impact on interest rates, therefore, is infinitesimal.

An analysis of title XI guarantee commitments as a share of total funds raised in U.S. credit markets shows that net new Title XI commitments were less than 0.1 percent or 1/1000th of the total net credit funds raised in 1981. While aggregate Federal involvement in proportion to the total credit market increased by 35 percent during the period 1972–81, title XI's relative proportion decreased by 60 percent in the last 5 years (1976–81) compared with the previous 5 years (1970–75). It has not distorted the credit markets therefore because new commitments have accounted for a decreasing percentage of the volume of new credit funds available. Title XI is not part of the uncontrolled expansion of Federal credit program.

Last, as Mr. Alan Greenspan of Townsend-Greenspan & Co. testified before the Senate Budget Committee's Federal Credit Task Force, the real distortion of the credit market by Federal participation occurs from direct Federal borrowing, either for its own use or in connection with Federal credit assistance programs with subsidized rates. As he noted, such borrowing differs from private borrowing in a fundamental way: the demand for funds by the Federal Government is wholly inelastic—absolutely insensitive to interest rates. No matter what the interest rates, the Federal Government must borrow to meet its commitments. Private borrowers, on the other hand are generally sensitive to interest rates. When rates go up, there is a pronounced contraction in demand for private credit and a delay in entering the credit market until interest rates decrease. Title XI is in those respects exactly like private borrowing, and unlike Federal borrowing. Other loan guarantee programs such as those run through the Federal financing bank at fixed, lower-than-market rates, contribute directly to the "crowding-out" effect.

Distortion of the credit market by Federal participation moreover is unhealthy where there are fewer total available funds than are demanded for capital investment in which case those ready and willing to invest in capital equipment may be "crowded out" by direct Treasury borrowings and Federal credit programs. Since, as shown above, every single title XI guaranteed dollar is put into capital equipment, and since it is highly interest sensitive, there is no "crowding out" in the case of title XI. The users of title XI financing are in fact the investors in capital equipment who would otherwise be crowded out.

One of the great disappointments of the tax cut to date has been the failure of the business community to reinvest the dollars retained by it in capital equipment. No such problem would occur with title XI, since demand for fully secured title XI guarantees remain strong, significantly in excess of the statutory authorization and far greater than the amount at which OMB has administratively limited the program to this fiscal year and section 4 of S. 2336 would limit the program in fiscal year 1983.

Title XI, moreover, rather than disrupting market forces enhances them. The merchant marine industry is highly capital-intensive. Accordingly, entry costs are exceedingly high relative to other industries. Free market forces work better as perfect competition is approached. Title XI enhances competition by facilitating entry.

Allocation of Credit.—Certainly, it can be said that title XI intervenes in the credit market by channeling funds to those who would not have otherwise obtained them. If title XI did not, there would be no need for the program. Title XI gives access to the U.S. long-term bond markets to companies, including smaller, independent entrepreneurial companies who are prepared to invest in productive capital equipment and who would not otherwise have such access. If title XI were eliminated or substantially eroded, as has been the case this past year, either less U.S. shipbuilding would occur—or large companies with access to the long-term capital markets would, to some extent, take up the slack. And much of that building would be transferred abroad. In that case, as we show later, the national defense shipbuilding base would be seriously harmed, and positive economic growth stifled. In addition, increased concentration would result in an industry now characterized by small- and medium-sized businesses.

The Effect on the Economy.—The Temple, Barker & Sloane study shows, in summary, that over 1,190,000 man-years of employment, or an average of 99,000 jobs annually, and $76.6 billion in revenues were generated by the title XI program during the period fiscal years 1970–81. For each dollar guaranteed (not borrowed) by the Government under title XI, a total of $4.70 of revenues is generated throughout virtually every sector of the United States. Three distinct types of positive impacts on the U.S. economy are generated: (a) direct impacts, (b) indirect impacts and (c) induced impacts. Direct impacts are the wages, other costs and profits plus the materials purchased by shipyards for title XI shipbuilding. During the period fiscal years 1970–81, $16.3 billion (in 1981 dollars) and 277,000 many-years of employment were generated by title XI. Indirect impacts are the goods and services purchased by suppliers to produce materials sold to shipyards and successive rounds of interindustry purchases. For each dollar of direct revenues another dollar of indirect revenues is generated; for each shipyard employee, another 0.8 jobs are created in the shipyard support/supply industry. During fiscal year 1970–81, $16.3 billion (in 1981 dollars) in indirect benefits and 220,000 man-years of employment were generated. The combined direct and indirect impact of title XI during the fiscal years 1970–81 period was $32.6 billion and 497,000 man-years of employment.

The induced impact represents the results of the wages of direct and indirect employees when spent by their households and then respent throughout the economy. For each dollar of direct and indirect benefit, $2.70 is generated as induced benefit, and for every direct and indirect job created by title XI another 2.5 jobs are induced by the direct and indirect incomes generated in the economy.

In addition to the positive impacts of Title XI shipbuilding, the ships built under title XI themselves have significant positive impacts. In 1980, the title XI fleet generated an estimated $4.8 billion in revenues and employed about 37,000 people ashore and afloat. This beneficial impact continues, moreover, each year for the entire life of the Title XI-built vessels.

National Defense Implications.—The title XI program is vital to national defense in two distinct respects: it contributes to the maintenance of a shipbuilding and supplier base which is essential for construction of naval vessels; and many of the vessels constructed under the program are available as naval auxiliaries.

Shipyards cannot maintain their work forces and other facilities while waiting for a naval shipbuilding program to come on stream without commercial construction. The title XI program is essential to commercial construction and cut-backs in title XI financing, including the elimination of drilling vessels, are threatening the closure of some yards and serious cut-backs in force by others. Without title XI, these yards will be faced with a loss of skilled employees and depletion of the supplier base needed for naval construction. Some of that has already occurred. While we have not quantified the amounts, we are confident that the unemployment costs associated with shipyard layoffs and closures are significant now and will only get worse without correction of the title XI problem. These costs are not contingent, they are real, and have direct adverse budgetary and economic impacts. Construction of title XI vessels, including drilling vessels, keeps shipyard work forces in place and spreads out overhead which would otherwise have to be paid for by the Navy in its own shipbuilding program.

Many vessels privately financed with the help of the title XI program are available to the Navy as auxiliaries and contribute substantially to the sealift capacity in both peacetime and in emergency situations. Thirty-four title XI-built vessels are now in service under charter to the Military Sealift Command. We wish to emphasize that these privately built vessels continue to be available for military use even if, as has happened, the original vessel owner goes bankrupt. As noted above, thus far the combination of preferred mortgages and the user-funded ship financing fund has covered such defaults. Nevertheless those vessels are available for national defense purposes with no expenditure of government funds.

If title XI's contribution to the national defense shipbuilding base and naval auxiliary fleet, all without cost to the Government, were eliminated and the cost transferred to the Defense Department budget, it would result in a substantial increase indeed.

SECTIONS 3 AND 4 OF S. 2336

Section 3 of S. 2336 would prohibit the Office of Management and Budget or any other Executive Office or Department from unilaterally limiting the amount of vessel financing guarantees which may be issued under title XI. However annual authorization limitations on title XI would be imposed for the first time and section 4 would set $675 million as the fiscal year 1983 limitation. We applaud the intent of S. 2336 to reassert Congress' right to authorize loan guarantees, but are greatly dismayed by the $675 million limitation. Moreover S. 2336 does not go far enough because it fails to increase the overall statutory ceiling.

Let us first address the reasons why the amount of increase in the statutory ceiling are warranted and necessary. At the present time the Maritime Administration lists applications for new title XI projects of over $4 billion. Of that amount, the Temple, Barker & Sloane study concludes that about $3.5 billion are active, viable applications. Moreover we believe that many new applications have not yet been filed which would have been if the future of the program had not been placed in doubt by the Office of Management and Budget. There is less than $1.5 billion in statutory authority left—more than $2 billion less than applications presently on file. One additional billion is needed at the very least to assure the continuation of the program. That would allow only very modest growth over a 3-year period.

Next, the $675 million annual limitation is wholly inadequate. Because of the OMB-imposed ceiling or, if enacted, the $675 million limitation in section 4 of S. 2336, TBS has estimated that $1.9 billion of the $3.5 billion in current active projects (for which title XI applications are on file) will be subjected to delay and possible cancellation over the next 2 years. Half of this business could be placed with foreign yards and the vessels so built operated with foreign crews. This, in turn, could expose more than 31,000 man-years of shipyard labor to lay-off; more than 133,000 jobs throughout the economy to loss; and cost the U.S. economy over $9.1 billion in revenues. Despite the fact that $675 million is 10 percent higher than the $600 million OMB asked for, it still represents a more than 50-percent cut in the program and a disincentive to an economy which is ailing as a whole and which, insofar as U.S. shipbuilding is concerned, is a near disaster. In our view, rather than looking for ways to cut the program, someone ought to be looking for a way to expand it.

Shipbuilding is a long lead time industry. A decision to build a ship today means that that ship will not be delivered for some 2 or 3 years and thus long-term financing will not be needed until delivery. Yearly authorizations, unless done 2 or 3 years in advance, destroy the value of the title XI program to the shipowner. He needs to know when he decides to build the ship if there will be title XI funds available in the year in which he puts the long-term financing in place. He cannot decide to build the ship, by and large, if he does not know whether the funds are going to be available when it is delivered. The traditional method whereby title XI was authorized on a 2–3 year basis allowing the market place to regulate the amount of guarantees issued within any year in the overall statutory ceiling has worked well.

If for overall credit control purposes, it is necessary to limit on a yearly basis the amount of title XI funds which may be issued, we urge the Committee to do so on a 3-year basis so that in any given year a company wishing to build a ship can gauge for itself whether funds will be available in the year in which it needs the money. To that end, in connection with increasing the statutory ceiling, the increase in authorization could be staged in $1 billion/year increments, that is to $13 billion in fiscal year 1983, $14 billion in fiscal year 1984, and $15 billion in fiscal year 1985. That satisfies any need for overall credit controls while at the same time providing barely enough funding for the backlog of applications which already exists.

SUMMARY

In summary, shipbuilding is a highly capital-intensive, long leadtime industry. Financial planning requires that a shipowner know at the onset of the project that funds will be available when the ship is delivered. The traditional title XI authorization process whereby the authorizing committees have adjusted the statutory ceiling at approximately 3-year intervals has worked well. Yearly authorizations, unless done 2 or 3 years in advance, would undermine the whole program. Within the authorization level, the market for capital equipment has set reasonable annual limitations. The $675 million limitation set by section 4 of S. 2336 would cut shipbuilding in the United States because it is far too low to accommodate the present demand. The statutory ceiling must be increased by at least $3 billion. Since the program has had only positive economic and budgetary consequences and since, as shown, cut-backs in the program will inevitably have immediate adverse economic and budgetary consequences, we recommend the title XI ceiling be increased by $3 billion, in yearly increments of $1 billion per year for the next 3 fiscal years, and that section 3 of S. 2336 be retained.

Attachment.

ITALIC SHOWS DIFFERENCES

PROPOSED AMENDMENT TO S. 2336

Delete Sections 3 and 4 and insert in lieu thereof the following: Sec. 3. Section 1103(f) of the Merchant Marine Act, 1936 (52 Stat. 969), as amended (46 U.S.C. § 1273(f)), is amended to read as follows:

> "The aggregate unpaid principal amount of the obligations guaranteed under this section and outsanding at any one time shall not exceed *$13,000,000,000 in fiscal year 1983, $14,000,000,000 in fiscal year 1984, and $15,000,000,000 in fiscal year 1985,* of which $1,650,000,000 shall be limited to obligations pertaining to commercial demonstration ocean thermal energy conversion facilities or plantships guaranteed under section 1110 of this title, and of which $850,000,0000 shall ~~be limited to obligations pertaining to~~ guarantees of obligations for fishing vessels and fishery facilities made under this title. *No application that meets the standards and criteria of this title, the approval of which will not cause the aggregate unpaid principal amount of the obligations guaranteed under this section and outstanding at any one time to exceed the dollar limitations herein, shall be denied or deferred.*"

Senator GORTON. Mr. Sclar, given the nature of the time and the fact that there is another witness after you, I would appreciate it if you could summarize rather than simply reading your statement. The written statement will be included in the record.

Mr. SCLAR. Fine.

My purpose today is simply to underscore the results of a recent study we have conducted on the economic impact of the title XI Federal ship financing guarantee program. The study findings have been provided to you by the title XI committee.

In brief, our analysis confirms what we have observed. The study demonstrated the title XI program is an effective, high quality, user-paid program and that it is essential to the continued viability of American shipping and shipyards.

The program has achieved its objective of providing U.S. shipowners with access to private capital markets at competitive interest rates and on terms that reflect the long lifetime of the vessels. It has done that along a number of key dimensions.

Title XI has supported projects of the highest quality governed by stringent approval criteria.

It has created a portfolio of sound marine projects that spreads the risk and helps shipowners tap the U.S. long-term capital markets for vessel finance.

User fees have been set at levels adequate to fully cover all the program's operating costs and the few losses that have occurred to date generating a surplus which is has created retained earnings of $241 million in the fund.

The title XI program is flexible and based entirely on market demand for ships and on market rates for long-term funds. It is crucial to recognize that shipowners issuing title XI guaranteed bonds are sensitive to interest rates, as demonstrated in the attached graphs, providing a self-limiting cap on the volume of bonds issued.

The economics benefits to the Nation have been substantial. Between fiscal year 1970 and fiscal year 1981 title XI guarantees generated 277,000 man-years of shipyard employment, a total of 1.2 million man-years of employment throughout the economy, and the $16 billion—1981 dollars—of title XI projects guaranteed during this period provided estimated national revenues of $76 billion.

These broad economic benefits are now threatened. Proposals to restrict annual title XI guarantee authority to levels of less than $1 billion would result in cancellations or delays in marine investments and would shift a substantial portion of these projects to foreign shipyards.

The record shows that new title XI commitments have exceeded $1 billion in 9 out of the past 12 years.

Applications for title XI guarantees on vessels worth $3.5 billion were outstanding at the beginning of fiscal year 1982.

Long-term funds cannot be obtained by many shipowners without title XI. Shipowners who can float nonguaranteed bonds, such as large oil companies, generally do not use the program.

Long-term financing for vessel construction is available on more attractive terms from foreign shipyards which benefit from Government subsidized export credits.

The proposed $675 million annual level of guarantee authority in fiscal year 1982 and fiscal year 1983 would place some $1.9 billion of projects at risk. These projects at risk threaten the loss of more than 30,000 man-years of shipyard employment, over 130,000 man-years of total employment and some $9 billion of revenue in the national economy.

There is no benefit to the economy, to the Treasury, to vessel owners, shipyards, or their employees in placing this $1.9 billion in projects at risk due to an arbitrary annual limitation in title XI guarantee authority.

If the title XI program is permitted to continue functioning in its traditional market-based fashion, major benefits will accrue to the economy. Shippers and customers will have the ships, drilling vessels, service craft, barges, tugs, and dredges they need to remain competitive. Shipyards will have additional work available to maintain their capacity and productivity. In short, the Nation's transportation, industrial, and defense objectives will be served.

I thank you for the opportunity to provide my views.

[The statement follows:]

STATEMENT OF MICHAEL L. SCLAR, VICE PRESIDENT AND DIRECTOR, MARITIME GROUP OF TEMPLE, BARKER & SLOANE, INC.

I am Michael Sclar, vice president and director of the maritime group of Temple, Barker & Sloane, Management Consultants of Lexington, Mass. I am here at the request of the committee for title XI vessel financing. I am accompanied by Messrs. Brent Dibner and David Bovet of the TBS maritime group.

My purpose today is to underscore the results of a recent study we have conducted on the economic impact of the title XI Federal ship financing guarantee program. The study findings have been provided to you by the title XI committee.

Our analysis of title XI confirms what we have observed in more than a decade of consulting service to U.S. ship operators and American shipyards. The study demonstrated that the title XI program is an effective, high quality, user-paid program, essential to the continued viability of American shipping and shipyards.

The program has achieved its objective of providing U.S. shipowners with access to private capital markets at competitive interest rates and on terms that reflect the long lifetime of the vessels. Title XI has helped finance over 7,000 vessels. How has this unique success been achieved?

First, title XI has supported projects of the highest quality, governed by stringent approval criteria. This is evidenced by the extremely low rate of defaults and by the fact that the program's contingent liabilities have never required funds from the Treasury.

Second, by creating a portfolio of sound marine projects, title XI spreads risk and helps shipowners tap the U.S. long-term capital markets for vessel finance.

Third, user fees have been set at levels adequate to fully cover all the program's operating costs and the few losses to date. These fees have generated the Federal ship financing fund, which today has retained earnings of $241 million.

Fourth, the title XI program is flexible, based entirely on market demand for ships and on market rates for long-term funds. Experience has shown that the shipowners issuing title XI-guaranteed bonds are sensitive to interest rates, thus providing a self-limiting cap on the volume of bonds issued.

The economic benefits to the Nation have been substantial. During the fiscal year 1970 to fiscal year 1981 period, vessel construction with title XI guarantees generated 277,000 man-years of shipyard employment and a total of some 1.2 million man-years of employment throughout the economy. The $16 billion (1981 dollars) of title XI projects guaranteed during this period provided estimated national revenues of $76 billion.

These benefits reflect the extensive interindustry linkages between shipbuilding and other economic sectors, and the household expenditures generated as a result of worker incomes. Both the direct impact and the indirect effects of title XI-assisted vessel construction are widely distributed along the coastal and inland regions of the country.

The operation of the fleet of vessels built with the aid of title XI guarantees also provides revenues and employment over the lifetimes of the vessels.

These broad economic benefits are now threatened. Proposals to restrict annual title XI guarantee authority to levels of less than $1 billion would result in cancellations or delays in marine investments and would shift a substantial portion of these projects to foreign shipyards. As evidence: The record shows that new title XI commitments have exceeded $1 billion (1981 dollars) in 9 out of the past 12 years.

Applications for title XI guarantees on vessels worth $3.5 billion were outstanding at the beginning of fiscal year 1982.

Long-term funds cannot be obtained by most shipowners without the title XI guarantee. This is due in part to restrictions placed on certain investors, such as pension funds, who are limited to government-guaranteed bonds.

Shipowners who can float non-guaranteed bonds, such as large oil companies, generally do not use the title XI program because of the guarantee fees involved.

Long-term financing for vessel construction is available on more attractive terms from foreign shipyards which benefit from government-subsidized export credits.

The proposed $675 million annual level of guarantee authority in fiscal year 1982 and fiscal year 1983 would place some $1.9 billion of projects at risk. These projects at risk threaten the loss of more than 30,000 man-years of shipyard employment, over 130,000 man-years of total employment, and some $9 billion (1981 dollars) of revenue in the national economy.

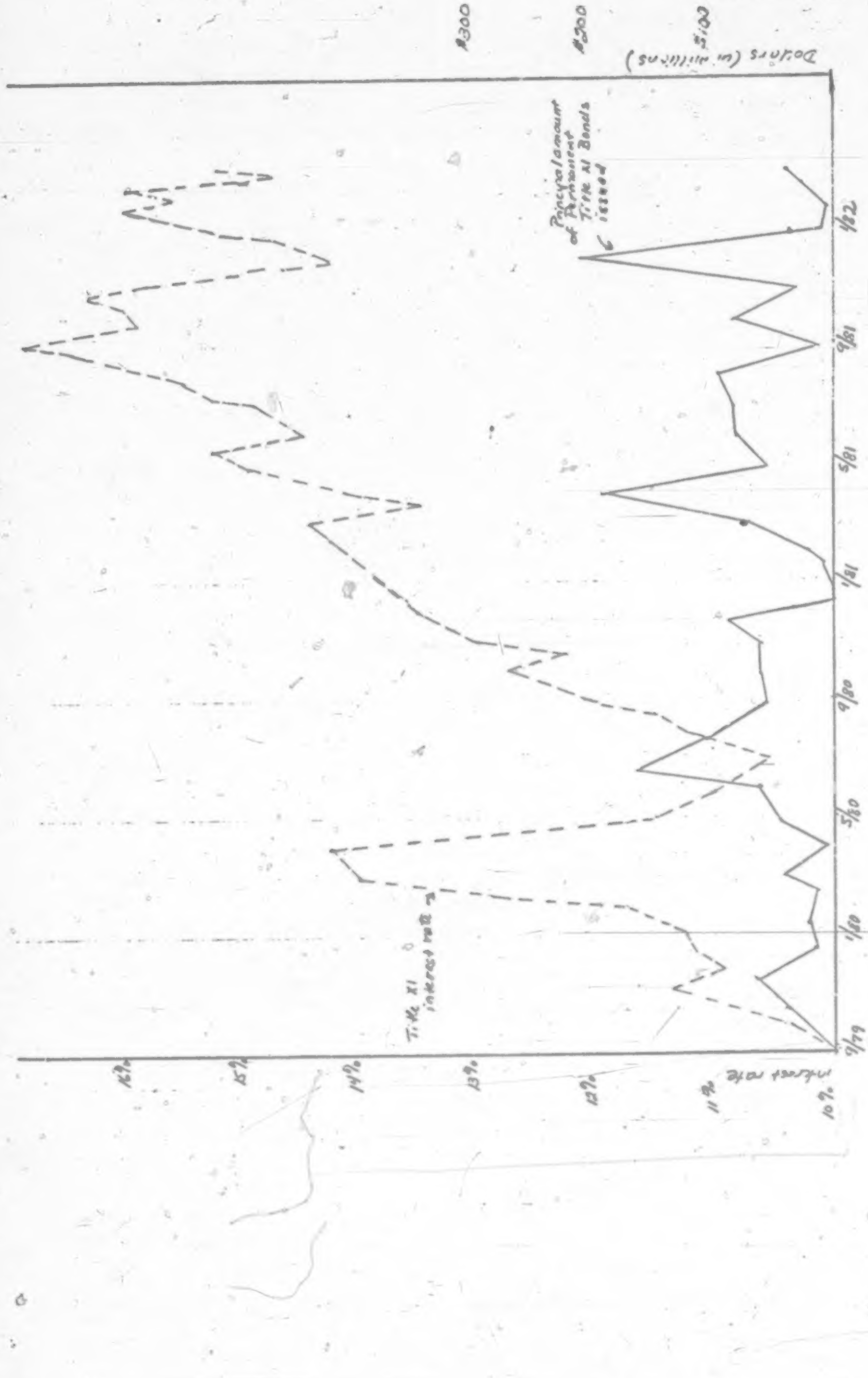
There is no benefit to the economy, to the Treasury, to vessel owners, shipyards, or their employees in placing $1.9 billion in projects at risk due to an arbitrary annual limitation in title XI guarantee authority.

The title XI program has accomplished its goals while supporting key government policy objectives. Its record of full cost recovery through user fees paid by shipowners advances the administration's goal of allocating the expense of government services to the beneficiaries. Title XI does not "crowd out" private sector borrowing; it is long-term private sector borrowing in support of major capital investments. The equity provided by the shipowner enables title XI to help mobilize private capital resources.

If the title XI program is permitted to continue functioning in its traditional market-based fashion, major benefits will accrue to the economy. Shippers and customers will have the ships, drilling vessels, service craft, barges, tugs and dredges they need to remain competitive, Shipyards will have additional work available to maintain their capacity and productivity. In short, the Nation's transportation, industrial, and defense objectives will be served.

I thank you for the opportunity to provide my views to this subcommittee. I would be pleased to respond to any questions.

Attachment 1



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Senator **Gorton**. Mr. Sclar, when you say the Title XI is essential to the continued viability of American shipyards, is that to suggest that no new building will occur without it?

Mr. **Sclar**. Without any, there would probably be some building occurring. Without any title XI there would be serious curtailments in the total amount of shipping and shipbuilding activities in the country. Most of the program would be lost to overseas and much would be lost in total.

Senator **Gorton**. Probably measured in the billions of dollars?

Mr. **Sclar**. Yes, sir.

Senator **Gorton**. Since these are Federal guarantees, and the actual lending comes from the private market, who will borrow that money if you are not using it and the free market determines who that money goes to? Or to reverse that question, who isn't able to borrow money because you are, in effect, first in line by reason of the Government guarantees?

Mr. **Fellows**. Could I respond to that, Mr. Chairman?

Senator **Gorton**. Sure.

Mr. **Fellows**. Maybe I can speak from our own situation. We are a benefactor of title XI and in our view it allows us to compete with the giant companies. What you are going to lose is the small- to medium-sized company. The loss of title XI will in effect be anticompetitive.

Senator **Gorton**. My question is, in the economy as a whole when you get to borrow $100 million because it is guaranteed by the Federal Government somebody else doesn't get to borrow that money somewhere in the economy, probably outside of your area. Who is it? Who is it that gets taken out?

Mr. **Mills**. Mr. Chairman, I think that you will find that the title XI bonds are bought in hugh proportion by pension funds who are restricted very narrowly to either direct Treasury obligations or Government-guaranteed obligations.

So if title XI were eliminated you would shift I think those purchases just to other Government guaranteed or other direct Treasury obligations. Unless you could eliminate all direct Treasury borrowing and all guaranteed programs, you would not have this effect of getting to I guess what you would say is the end of a line. There just is no risk capital in highly risky ventures purchased by the pension fund.

Senator **Gorton**. By how much does title XI affect the interest rates that you have to pay as against what you would have to pay to borrow the same amount of money without a guarantee?

Mr. **Fellows**. It impacts the interest rates to this effect. A medium-sized company such as our own can borrow at rates equivalent to say an A-rated bond. More importantly what title XI provides is an extended term as well as interest rate considerations.

Senator **Gorton**. Can you quantify what your interest rate is in your estimation as opposed to borrowing without a Federal guarantee?

Mr. **Fellows**. In our own particular situation it would probably make a 2-percent differential.

Senator **Gorton**. But that amounts to a Government subsidy, doesn't it? How can you say that it is not a subsidy. It may not be a very good one but it is a subsidy, is it not?

Mr. **Fellows**. Well, that can be a term applied to it, Mr. Chairman. Since it does operate in the free market as opposed to a fixed rate we will not borrow under title XI when interest rates are high. We will only borrow when interest rates are acceptable.

I think one of the considerations that title XI does provide, and I think you have to address this fact, is it provides an adequate term to repay the vessel through normal channels of financing. Those lenders are not available to us, absolutely not available to us. We would be forced into borrowing from the bank which is under terms of 7 years or less.

Senator **Gorton**. We do have some correspondence, Mr. Fellows, from an operator of offshore supply vessels in the gulf who contends that the business already has excess capacity and that title XI is encouraging an entry of fragile and unnecessary new businesses and that he therefore doesn't like it. How do you react to that criticism?

Mr. **Fellows**. From time to time I guess I would agree with that analysis. I think on balance title XI provides the stability to the marketplace. The river industry today is an oversupply condition. It would be naive to suggest anything else.

The supply of equipment and the demand for equipment is kind of like a river. It is high part of the year and low other parts of the year. That need will come back. We need to have as an industry the knowledge that financing capabilities will be available 3 years hence so that we can make our plans today. To make an allotment for fiscal year 1983 only will be inhibiting to my industry. I made decisions 1 year ago for fiscal year 1983. I am looking at 1984 and 1985 at the present time.

Senator **Gorton**. That leads very logically to my next question. Since these of course are Federal Government-guaranteed programs and since we have to have some way rationally to determine how much credit should be allocated in the form of guarantees, how can we subject title XI to some kind of budgetary control and limitation and still allow the industry to make long-range plans?

Mr. **Fellows**. Well, I think you have to do it in multiyears at a minimum of 3 years. Our suggestion is $1 billion per year for the next 3 years which fairly tracks with the past history on a price suggested basis.

Senator **Gorton**. If we set them say for 3 years in advance in that fashion aren't applicants still going to compete for what is still scarce authority in a way which makes long-range planning somewhat difficult?

Mr. **Fellows**. It will make it difficult. Obviously we would like a higher statutory ceiling. But 3 years is possible to work within, 1 year is impossible to work within.

Senator **Gorton**. During the course of the last year with tight title XI authority have not some operators been able to arrange financing in which title XI covers only half or maybe 60 percent of principal obligations rather than the usual 87.5 percent?

Mr. **Fellows**. Well, I think Maritime increased the amount of equity required, to 25 percent in most cases. Barges historically were 87.5-percent Government guarantee and I think that has been reduced to 75.

Senator **Gorton**. Is that an effective way of extending scarce loan guarantee authority?

Mr. **Fellows**. I would support that because I personally believe in a high capital industry. You should discourage high levels of leverage, and a 25-percent equity contribution is a fair contribution and I would support that.

Mr. **Mills**. Mr. Chairman, just one statement.

Senator **Gorton**. Go ahead.

Mr. **Mills**. Thank you. You have remarked that you have not heard of differentials much less than 2 to 1 in shipbuilding costs and indeed up to 3 to 1 and 4 to 1, et cetera.

One thing for which Title XI is vital is the offshore rig industry. The price differential as between in the United States and abroad is nowhere near two to one. Indeed, by the time you factor in the transportation cost of building a rig overseas and moving it, say, to the U.S. gulf, with title XI the yards are highly competitive. Indeed, half of the rig population, which makes up a good deal of the shipyard employment over the last 10 years, half of the offshore rig population was built in the United States.

Now the immediate effect of OMB's ceiling was, of course, to eliminate rig building under title XI and in effect OMB has driving that construction offshore. So it is not true that the shipbuilding industry in the United States is absolutely uncompetitive in all aspects.

Senator **Gorton**. That is an important point. I am glad you made it.

Thank you very much.

Mr. Drozak.

STATEMENT OF FRANK DROZAK, PRESIDENT, SEAFARERS INTERNATIONAL UNION AND PRESIDENT, AFL-CIO'S MARITIME TRADE DEPARTMENT

Mr. **Drozak**. Thank you, Mr. Chairman.

Mr. Chairman, I appreciate the opportunity to share our views on S. 2336, a bill to authorize appropriations for maritime programs for fiscal year 1983.

We strongly support the national maritime policy that is the basis of the Merchant Marine Act of 1936 as amended. This legislation established the national goal of development and maintenance of an adequate and well-balanced American merchant marine capable of carrying a substantial portion of our foreign trade. It established such programs as the operating differential sudsidy—ODS—and the construction differential subsidy—CDS—in order to achieve this goal.

The common view of the legislative history of this act is that Congress intended substantial portions to mean 50 percent of our trade. Given that we are presently carrying a mere 3.6 percent of our trade, it is safe to say that something has gone wrong.

We agree with those who say that the time has perhaps come to take a look at these programs. Maybe they are not the best of all possible ways to achieve the goal they were set out to achieve. But we believe absolutely that the overall goal remains as valid in 1982 as it was in 1936.

The Nation's security requires that we have a substantial merchant fleet. Indeed, defense experts will tell you that today's fleet is almost totally inadequate to meet significant wartime obligations. It has become well known that we don't have the sealift needed to supply our oversees forces. Of equal importance, in our view, is the fact that we don't possess a dry bulk fleet to carry the raw materials that are essential to our industries.

For this reason alone we think it is extremely unwise to tamper with the existing programs until the full implications are understood. This is not simply one more industry that should "sink or swim" based on market factors alone. As the Soviet Union understands all too well, the merchant marine is a major instrument of national policy.

A year ago we had an inadequate fleet. There were some 537 active ships in the privately owned deep sea fleet. As of January 1 this year, according to MarAd's monthly report, we had dropped to 502 ships; 1,600 seafaring jobs were lost in the first year of this administration. Clearly even with our existing programs something is terribly wrong.

When this administration came to office we were hopeful that things were going to be improved. It seemed to us that this administration, unlike the two that went before it, was going to act swiftly and boldly to give this country the maritime program that we so badly need.

We felt that our hopes were reasonable. As a man who understands the importance of national security, we thought President Reagan would be a President who would quickly grasp the need to revive this ailing industry. His statements as a candidate led us to this conclusion. Both his 7-point maritime program and his statement of support for the Jones Act sounded good. We were especially encouraged that he seemed to recognize the need for a positive national cargo policy. We were further encouraged by Secretary Drew Lewis' statement of strong support for existing cargo-preference programs.

More than 1 year has passed and we are no longer hopeful. The record to date is far from encouraging. The numbers speak for themselves.

Almost immediately after taking office this administration moved to close the U.S. Public Health Service Hospitals. In addition to seafarers, these hospitals had provided health care to a variety of groups, including the Coast Guard, the Military Sealift Command, veterans, and civil service employees. In closing the hospitals, the Government has continued to provide care for all parties except maritime labor, the fourth arm of defense.

Since the hospitals closed, Mr. Chairman, in October 1981, the cost of providing medical care is exceeding $1.2 million a month for S.I.U. members alone. This cost is being met from the union's welfare plans. Mr. Chairman, the strain of such a cost is enormous. We believe that the Government ought to make provisions for reimbursing our plans for this cost giving us the same treatment as others who were using these hospitals prior.

Beyond the Public Health Hospital question, the administration has gutted the construction differential subsidy program. It is well on its way to undercutting the operating subsidy and the title XI loan guarantee.

What is worse, Mr. Chairman, is there is nothing visible on the horizon that will improve things. We hear a lot of promises about the promotional program, but the date of its appearance keeps being moved back.

We are, therefore, extremely concerned by some of the major policy changes implied in the authorization bill you are considering.

This year's authorization bill calls for $454 million for the operating differential subsidy program. ODS is aimed at providing equity for the U.S. shipping in the international trade in much the same way that most other maritime nations provide direct or indirect subsidies for their fleets. The economic benefits of the ODS program are numerous.

A recent study by the Maritime Administration revealed that the $1.9 billion expended in operating differential subsidy between 1970 and 1978 generated $11.6 billion in output. It provided 196,000 man-years of employment in the maritime industry. ODS is an essential part of our Nation's maritime philosophy at this time. We believe that the ODS program should continue to be funded at the highest level.

We are deeply concerned about the lack of funds for the construction differential subsidy, the CDS program. In the above-mentioned MarAd study it was determined that the $1.4 billion made available for CDS during the same period has led to the construction of vessels and maritime equipment valued at $4.2 billion. It has provided 136,000 man-years of shipyard employment.

Most importantly, national security requires that we maintain a shipyard mobilization base. Anyone familiar with the industry knows that our yards are having terrible problems. There are those who think the naval buildup will be enough to save our shipyards. The experts in the field tell us that naval work alone is not enough.

Accordingly, we think it is foolish to abandon the CDS program until a clear, workable, alternative program has been announced. In the absence of such a program we strongly oppose the language in S. 2336 which makes foreign building a permanent fact of life for U.S.-flag operators receiving ODS.

We are also deeply concerned with the proposal to place a ceiling on the annual obligations of the title XI loan guarantees. This program operates without cost to the Government. It has made possible the construction of over 2,700 vessels, including 262 deep sea vessels and more than 2,300 inland waterway vessels.

In 1980 alone, title XI ships generated an estimated $4.8 billion in operating revenues. U.S. vessels built with the assistance of title XI guarantees also employed about 37,000 persons ashore and afloat with a $900 million payroll.

The $675 million annual authorization ceiling, combined with the Maritime Administration's 75-percent guarantee level, can finance only $900 million of construction in fiscal year 1982. Assuming that only an additional $675 million will be made available in fiscal year 1983, some $1.8 billion worth of projects could be financed during 1982 and 1983. However, because the October 1, 1981, active application backlog totaled $3.7 billion in 1981 at least $1.9 billion cannot be financed during the next 2 years. Furthermore, our already inadequate shipbuilding capability will be further weakened by the lack of commercial construction.

In conclusion, Mr. Chairman, we would urge this subcommittee to practice restraint. When the Reagan administration came into office you very wisely waited to hear what their views were on regulatory reform before you put your own legislation together.

We would urge you to show the same wisdon in not changing existing promotional programs until the administration's alternatives have been proposed and carefully examined.

Since the funding levels authorized by S. 2336 have the effect of altering existing policy, we would urge you to consider instead the figures in the House maritime authorization bill. In addition, we would urge you to authorize a program to reimburse the union's welfare plans for the costs that have resulted from the closing of the Public Health Hospitals.

In addition, we would urge you to press the administration to reveal the details of this promotional program as quickly as possible. To work such a program must include ways and means to preserve our essential shipyard mobilization base. It must also contain ways and means to achieve the goal of an active merchant fleet capable of carrying a substantial portion of our foreign trade.

Mr. Chairman, we remain, as always, willing and eager to do our part to work to turn this industry around.

Thank you.

Senator Gorton. Mr. Drozak, I would like to thank you for a thoughtful and an eloquent statement.

You leave me somewhat frustrated, however, in that last set of recommendations because while we don't have that overall, complete administration program, and I think you heard from me earlier when I attempted at least to speed it up, we certainly do have an administration program in the sense that they submitted a set of recommendations to us in these areas which you are covering. We have made a modest upward change in one area, in the title XI area. But in fact we have their recommendations.

It is the view, at least of the subcommittee chairman, that to attempt to go back, for example, to a significant CDS authorization, if it became reality, would just almost certainly invite the kind of vetos with which we were favored last year. What our real task is is to try to build a bridge in connection with something we can get done and something that will do something for the merchant marine at the same time.

Now given that perception, and maybe I am wrong of course, but given that perception you have recommended that we don't tamper with existing programs until an overall alternative which is workable is announced.

Specifically, you opposed that foreign building authority even though it seems obvious that no CDS is going to be made available for fiscal year 1983. Doesn't that sort of "cut off your nose to spite your face"? I mean, isn't that going to risk more jobs in your union? If we are faced with the fact that we are not going to have any money, shouldn't we allow the foreign building to take place?

Mr. **Drozak**. Mr. Chairman, if I may reply to that. I don't think building foreign-flag ships is going to create one more job or create one more ship unless there is a promotional program relative to our maritime industry. What Delta, and what APL, and CASO testified to here this morning, certainly I have an interest in both of those companies because I represent the people in them, but they are talking about midbodying ships.

I don't know of anyone and I haven't seen any proposal, Mr. Chairman, of anyone submitting to build foreign-flag ships at the present. Now my problem is this, that until we can get some kind of a sound program coming out, I don't think we should tamper with what we have presently got. If there is building in there, then certainly let's look at all of it then. But I don't believe in just saying let's go build foreign without some kind of a maritime policy, allied cargo, bilateral shipping agreements, et cetera. It all ties in together. Just one part of it will not do it, in my opinion.

It is like your regulatory bill, Mr. Chairman, and I support your regulatory bill 100 percent. I think it has been needed for many, many years. But it does not build another ship nor does it create another job. It is a house-cleaning job. As I testified over in the House side, I had hoped that that wouldn't be our maritime program bill.

Senator **Gorton**. Well, I hope not, too.

Mr. **Drozak**. But I want to make one thing clear. I am not opposed at the present, if that is what we have to do to replace those ships until we get a program going, then we have got to build them somewhere. But other than those ships that have been mentioned, and that is midbodying these ships, I don't know of anybody that has proposed to build any of these ships.

Senator **Gorton**. I just want to make it entirely clear, you don't want us to extend this authority to build overseas even if we are not going to have any CDS?

Mr. **Drozak**. Yes; I think we should have some CDS, Mr. Chairman, and let me tell you why. Foreign building is fine, but with the country and this world the way it is and the hostilities in all of these countries, even with the governments guaranteeing that there will be deliverey and no problems, I have a great concern as to the work force in these countries. If we have no mobility of building ships in this country that they wouldn't put a gun to our back on supplies or needed equipment that would be necessary to repair a ship once it is built or to say because of labor problems we are not going to deliver these ships. This is a concern that I think we all ought to look at.

I had proposed to this administration back last year to Mr. Drew Lewis and also to the President, and I also spoke to the metal trades and shipbuilders, and I thought the proper thing to do was to look at a one-on-one bill and see what it would do for a period of time. Maybe we could get the shipbuilding mobility base in this country more competitive. Then if we couldn't, then the opportunity would be that we would have to go there, but certainly we would have to have some kind of protection from the countries as to whether we would get our deliveries and also after deliveries will we be able to get our spare parts and the equipment necessary. If you close out manufacturing in this country, which will be done, then there is a possibility of never getting it back.

Senator GORTON. I have one last major question for you, and at least as far as the breakdown is concerned you may not be carrying these figures right around in your mind, but they are important to us and I would like you to submit them to us if you can. Senator Inouye also has questions for you to answer for the record.

Thank you very, very much, Mr. Drozak. We appreciate you being here.

Mr. DROZAK. Thank you, Mr. Chairman, for the opportunity.

[The following information was subsequently received for the record:]

QUESTION OF SENATOR GORTON AND THE ANSWER THERETO

Question. How many active U.S. seamen are there today looking for sea-going employment? How many jobs are available to them aboard U.S.-flag vessels? (For the record, could they break this down into types—masters, mates, engineers, and other crews?) How many of these jobs are available on U.S.-flag liner vessels?

Answer. According to the Maritime Administration's April 1, 1981 U.S. Merchant Marine Data Sheet, there are approximately 21,076 oceangoing billets available to U.S. seamen aboard the privately-owned and government-owned and government-leased U.S.-flag fleet. Since each billet supports two seamen, these 21,076 billets are providing jobs for 42,152 U.S. seamen. Compared to last year's figures, the number of billets, and therefore the number of jobs, is down significantly. On April 1, 1981, there were 23,368 billets available. This decrease of 2,292 billets translates into a loss of 4,584 seafaring jobs in a single year.

Details on the jobs by the categories, e.g., masters, mates, engineers, etc., are not readily available to the separate unions in the private sector. However, MarAd or the Coast Guard may have a more detailed breakdown. For the purpose of its published report, MarAd groups these categories under two general headings: Licensed and Unlicensed personnel. As of April 1, 1982, there were 6,281 licensed oceangoing billets listed, providing jobs for 12,562 licensed seamen, and 14,795 unlicensed billets providing jobs for 29,590 unlicensed seamen. It should be noted, however, that these figures do not necessarily reflect the unfilled billets resulting from the present idle status of a number of ships that are included in the MarAd list of active vessels.

As to the number of jobs available on U.S.-flag liner vessels, we do not have exact data. However, we know that there were 231 liner vessels active as of April 1, 1982. Assuming that the average vessel carries 12 licensed billets and 26 unlicensed billets, the total number of available billets would be 8,778 (2,772 licensed and 6,006 unlicensed).

A May 1982 survey we conducted of the major seafaring unions identified approximately 67,600 active members either employed or seeking seagoing employment. This number does not include the number of inactive members who have not worked recently and are therefore not on record with the unions. These inactive members would also be looking for sea-going employment if job possibilities existed.

Of the 67,600 active seamen, approximately 21,000 are licensed and 46,000 are unlicensed. This large labor pool contrasts sharply with the number of jobs available. The current 21,076 billets with its only 42,152 employed means that 25,446 seamen or "on shore" and waiting for new opportunities to arise. For unlicensed ratings, it is likely that the greater part of this excess number seeking work is composed of entry-level personnel (e.g., ordinary seamen, wiper or steward's assistant) who have had short-term employment or no prior employment in the maritime industry. Instead of new opportunities opening, we can see from the number of billets lost over the past year that their chances for employment and advancement in a sea-going career are decreasing rapidly.

QUESTIONS OF SENATOR INOUYE AND THE ANSWERS THERETO

Question. In your testimony, you testified since closing the Public Health Services Hospitals, the cost of providing medical care is exceeding $1.2 million per month for the SIU alone. You propose the government make provisions for reimbursing your plan for this cost. How do you propose the government reimburse your plans for this cost?

Answer. For nearly two centuries, from 1798 until 1981, the United States Government accepted responsibility for the medical care of U.S. merchant seamen, funding their health programs first through a tonnange tax and, more recently, through direct appropriations. It was in the national interest to provide adequate health care for seamen but that came to an abrupt end last year when the funding for the program was terminated. That action shifted the responsibilities for health care directly to the industry and has seriously strained resources to provide adequate coverage to eligible seamen. Medical costs for SIU members alone have steadily increased since the closure of the PHS hospitals to approximately $1.2 million per month presently with further increases projected.

In view of the fact that the retention of a corps of able-bodied seamen, in a viable U.S. Merchant Marine, still serves the nation's economic and security interests, we believe the government should reestablish its responsibility for seamen's health care. This could be accomplished through a return to allocating existing tonnage tax receipts to a scaled down PHS program or establishing a system through which seamen's health care expenditures are reimbursed. The mechanics of covered reimbursement would need to be worked out with the committee.

The options that could be considered include establishing U.S. Government contract with a health service organization, such as those operated jointly by labor-management trust within the maritime industry or through periodic billing by authorized plans for reimbursement of covered medical costs provided to eligible seamen. First, however, we feel it imperative that the government acknowledge its federal responsibility for the health and welfare of American merchant seamen.

Question. Do you believe that our present cargo preference laws are adequate to ensure that 50 percent of government-impelled cargo moves on U.S.-flags? Have you had any difficulty getting agencies to observe the 50/50 requirement?

Answer. It is quite apparent that the laws governing cargo preference are adequate, in principle, but our problem has been with compliance by Federal agencies. This is due to what I feel is a significant flaw in the law, an inability to enforce its statutes simply because of the lack of clarity as to the types of programs that should be covered and the absence of explicit authority in section 901(b) of the Merchant Marine Act of 1936 for MarAd to define which programs should include cargo preference provisions.

MarAd has had little success in having cargo preference provisions included in agreements for all Federal agency programs where it believes cargo preference is required. What MarAd has found is that agencies dispute its interpretation of cargo preference applicability.

Let me provide you with some examples of agency noncompliance with the cargo preference law.

URBAN MASS TRANSPORTATION ADMINISTRATION

An UMTA grant was responsible for the purchase of 400 articulated buses constructed in Germany and shipped to the United States. U.S. flag operators submitted bids to carry the buses, but were excluded when they should have received at least 50 percent of the cargo. Some of the buses were delivered to the United States in Soviet ships. It was not until the issue was brought before the Congressional Committee that U.S. flag participation was involved.

DEPARTMENT OF AGRICULTURE

The Commodity Credit Corporation (CCC) of the United States Department of Agriculture (USDA) instituted two new programs designed to encourgage agricultural exports. Through departmental rulemaking, both programs avoided cargo preference requirements. It is inconsistent that these programs are exempted when cargo preference requirements apply to other similar programs.

Last August, USDA concluded an agreement with New Zealand to sell excess supplies of butter, at below-market prices on concessional terms. USDA said that preference requirements did not apply since it was a "commerical sale" while MarAd had determined that this cargo was subject to cargo preference rules.

AGENCY FOR INTERNATIONAL DEVELOPMENT

The Agency for International Development (AID) has also exempted some of its programs from cargo preference requirements. AID moved to exempt the cash transfer program to Israel from cargo preference requirements. This has led AID to exempt other programs from preference compliance based in the same rationale, again reducing U.S.-flag participation.

DEPARTMENT OF ENERGY

A further example of compliance failure can be found in administration of the Strategic Petroleum Reserve (SPR). This program has consistently failed to meet cargo preference requirements since operations resumed in October of 1980. The Department of Energy (DOE) in a final attempt to ostensibly meet compliance levels has resorted to including shipments of Alaska oil against the cargo preference requirement. This is inconsistent with the law. Section 27 of the Merchant Marine Act of 1920, commonly known as the Jones Act, requires all domestic waterborne trade to move on U.S.-flag ships, which covers shipments of Alaska oil. The Cargo Preference Act requires a minimum of 50 percent of the foreign oil purchases to move on U.S.-flag ships.

GENERAL SERVICES ADMINISTRATION

Finally, the General Services Administration's recent purchase of Jamaican bauxite for the U.S. stockpile is an indefensible example of a government agency sidestepping compliance with the Cargo Preference Law. Anyone looking at the way the GSA went about this business can see that they had no intention of using U.S. Flag Service. The details of their original request favored a single company and a single site for the storage requiring a self unloading vessel, even though other sites, compatible with U.S. Flag bulk vessels, were available. The narrow selection of a single site thus led to U.S. Flag exclusion from the business. In addition, the time given operators to respond to the GSA request was absurdly short--less than two days.

We believe the problem can be solved in one or two ways: The President can issue executive orders directing all agencies to comply with the spirit as well as the letter of existing law. The Secretary of Transportation can exercise his authority as the President's maritime spokesman to ensure that Federal agencies observe the relevant laws.

[Whereupon, at 12:50 p.m., the subcommittee adjourned, subject to the call of the Chair.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

STATEMENT OF PETER J. LUCIANO, EXECUTIVE DIRECTOR, TRANSPORTATION INSTITUTE

Mr. Chairman and members of the subcommittee: My name is Peter J. Luciano. I am executive director of the Transportation Institute. The Transportation Institute is a nonprofit research and educational organization which directs its efforts towards the preservation and promotion of a strong marine transportation capability in the United States. Our 174 member companies operate U.S.-flag vessels in the nation's foreign and domestic shipping trades including the inland waterways and Great Lakes.

We appreciate the opportunity to express the views of the Transportation Institute on S. 2336, a bill to authorize appropriations for certain maritime programs under the auspices of the Maritime Administration and for the administration of programs under the Federal Maritime Commission for fiscal year 1983. As the members of the Subcommittee are aware, S. 2336 calls for the following expenditures: $454.01 million for the operating-differential subsidy program; $16.8 million for research and development; $71.013 million for operations and training; $6.516 million for reserve fleet expenses; $29.607 million for maritime education and training expenses; and, $10.378 million for the Federal Maritime Commission.

The Transportation Institute fully supports authorization of the funds requested in this measure as they are fundamental to the maintenance of U.S. maritime policy as mandated by the Congress in the Merchant Marine Acts of 1936 and 1970. Until the administration and the Congress restate U.S. maritime policy through the enactment of alternative programs, the Transportation Institute believes that the funds provided for in this bill are indispensable to the continued existence of a U.S.-flag merchant fleet.

The importance of the operating-differential subsidy (ODS) program cannot be understated. The ODS program currently supports no less than 33 percent (177 ships out of 531) of our merchant fleet. This 33 percent includes almost 60 percent of all U.S.-flag liner vessels. The ODS program helps provide U.S.-flag service in trade routes which are essential to the maintenance of a strong defense capability and which insure the flow of strategic materials to the United States. The President's stated intent to allow no additional ODS commitments at this time is of grave concern to the American maritime industry. The Institute urges that the subcommittee fund this vital program at the highest level.

Funding for one long-standing maritime program has been completely eliminated in the administration's budget request for fiscal year 1983. S. 2336 provides no funds for the construction-differential subsidy (CDS) program. The CDS program has accounted for over 40 percent of the merchant ships built in the United States over the last 10 years. During the period 1971-1980, 217 merchant ships were constructed in U.S. shipyards. Of these, 90 were built with the aid of construction-differential subsidy. Abandonment of this program could have severe repercussions on the Nation's ability to maintain a shipbuilding mobilization base.

Congress has repeatedly stated that a shipbuilding base is a vital component of our national security. U.S. shipyards are currently desperate for work. Only nine new vessels of over 1,000 gross tons have been contracted to be built in 1982. It is readily apparent that shipbuilding facilities will be idled and thousands of skilled shipyard workers will be unemployed. Although increased naval building will provide some work, it will not be nearly enough to compensate for the decrease in commercial construction.

The Transportation Institute is deeply concerned with the subcommittee's proposal to place a cap on new loan guarantee commitments under section 1103 (f) of the 1936 Merchant Marine Act, commonly referred to as title XI. The title XI program is essential to the maintenance of a shipbuilding mobilization base for national security. As you know, this worthy program is administered without cost to the public treasury and without appreciable distortion of credit markets. These loans are made through private institutions at free market rates and receive no Federal subsidy.

The title XI program thus, does not eliminate other investors from the market, but instead encourages increased capital formation in the United States.

Over the years, title XI loan guarantees have provided for the construction of thousands of ships, barges and offshore drilling rigs. This, in turn, has employed thousands of Americans in U.S. shipyards and support activities. A limitation on new guarantees would severely hamper efforts of U.S operators to obtain financing necessary for the modernization and expansion of the U.S.-flag fleet. The Institute, therefore, favors increasing the ceiling of the title XI program by $1 billion per year over the next 3 years, so as to arrive eventually at a ceiling of $15 billion.

The funds provided in this authorization bill are a minimal form of assistance in comparison with the direct and indirect aids other maritime nations offer to bolster their merchant fleets. Most major maritime nations view their merchant fleets as a basic ingredient of economic independence and national security and, therefore, provide some degree of special assistance.

During the 1970's, we witnessed the rapid expansion of state-owned fleets which need not make a profit and, thus, often use rate-cutting and other practices to underbid competitors. Argentina, Brazil, China, Iran, and the Soviet Union represent a few of these state-controlled fleets.

Many maritime nations offer tax breaks in the form of tax credits, accelerated depreciation, tax-free reserve funds, and duty-free imports of material necessary for ship construction. The 1970s also witnessed an increasing trend toward negotiation of bilateral shipping agreements and other cargo-sharing accords. With the rapid growth of state-controlled fleets, government-negotiated cargo-sharing agreements will become a leading form of maritime aid in future years.

With these points in mind, the Transportation Institute urges the members of this Subcommittee to begin formulating a new maritime policy for the United States. There are many opportunities and options for the United States to regain its maritime capability and to be the premier maritime power in the year 2000.

In conclusion, the Transportation Institute wishes to thank the members of this Subcommittee for their efforts to strengthen the U.S. maritime industry. The Shipping Act of 1982, supported by the subcommittee, is a fine step toward relieving the maritime industry of a regulatory burden which presently encumbers it. The funds contained in the authorization bill currently before the subcommittee members is another important step to help maintain what limited merchant fleet we have. We urge the Subcommittee to continue its efforts to develop a legislative program to restore the American merchant marine to the status required in the national interest.

Thank you.

STATEMENT OF JULIAN H. SINGMAN, PRESIDENT, MARITIME INSTITUTE FOR RESEARCH AND INDUSTRIAL DEVELOPMENT

Mr. Chairman and members of the subcommittee: I am Julian H. Singman, president of the Maritime Institute for Research and Industrial Development. The Maritime Institute is a nonprofit corporation of maritime companies operating U.S.-flag vessels in our Nation's foreign and domestic shipping trades and which are signatories to employment contracts with the International Organization of Masters, Mates & Pilots, ILA, AFL-CIO. We are grateful for this opportunity to present the views of our member companies on the coming year's budget proposal for maritime programs under the Maritime Administration.

First, we wish to state that we are gratified that, contrary to much speculation, the Administration has chosen not to ignore its existing contractual obligations under the operating differential subsidy program. It is our understanding that the proposed fiscal year 1983 outlay of $454 million is likely to be sufficient to meet these continuing obligations to United States-flag operators.

In evaluating the role of the operating differential subsidy program in our maritime promotional framework, we should bear in mind that it has been formulated, not as is often charged, to guarantee profits, but rather as an equalizer. ODS is designed to enable American vessel operators to better compete with foreign operators who, for the most part, receive even greater financial assistance from their own governments and who are not subject to the same type of restrictions and regulations as are American operators. In fact, it is becoming increasingly a fact of life that American operators must compete more and more with foreign state-controlled fleets, stringent cargo reservation laws, and economic incentives for foreign national flag fleets.

We must, therefore, strongly resist budgeteer charges that the operating differential subsidy program is a "grant" intended to keep an industry going. We must see to it that the uninformed realize that it is an equalization program to make it possible for American vessel operators to compete with foreign subsidies, foreign maritime discrimination and foreign fleets of state-controlled economies. Until such time as the United States adopts and implements a national cargo policy which results in the carriage of a substantial portion of American foreign trade on American ships, it is imperative that the operating differential subsidy program be kept in place and even expanded.

In this regard, we are extremely disappointed that the fiscal year 1983 budget request contains no funds for new operating differential subsidy contracts. Of course, we fully understand and appreciate the desire to reduce Federal spending and shrink the budget deficit in order to nurse the American economy back to health. However, it seems to us that the threatened end of the operating differential subsidy program as a means to encourage the operation of an American fleet, with nothing put forward in its place, is counterproductive to our national economic goals, as well as to our national defense needs. The operation of additional American vessels will generate additional tax revenues for the United States Treasury, while the earnings from American-owned foreign-flag vessel operations can be sheltered from U.S. taxes through the so-called subpart F provisions of the tax code.

Similarly, additional American vessels will mean additional jobs for American maritime workers and retention of a reserve pool of trained manpower available for national emergencies. Unemployment in our industry has been increasing. According to the Maritime Administration, there were 19,385 oceangoing shipboard jobs on privately owned American vessels as of December 1, 1980. One year later, the number of jobs dropped by 1,598 to 17,787. Due to the nature of our industry in which one seagoing job generally provides employment for two people, a loss of 1,598 jobs affects 3,196 workers.

Finally, the greater utilization of American vessels for the carriage of American foreign trade will improve our nation's balance of payments. A decrease in this deficit would help strengthen the dollar and would help offset the effects of lowered interest rates.

Again, let me assure the subcommittee, Mr. Chairman, that we do understand the budgetary constraints upon the Congress and the resultant reluctance to make available additional funds for new operating subsidy contracts. But if that is inevitable, then it is absolutely essential to the future operation and expansion of the American merchant marine, and indispensable to our economic and defense planning, that new and alternative approaches to the existing subsidy framework be considered and implemented.

One possible means of increasing the amount of funds available to American operators would be to exempt from Federal income taxes wages earned by American workers employed on U.S.-flag ships while on foreign articles. With such an exemption, wages could be rolled back so that each seaman could gross less, take home the same, but each operator would be required to pay less. This in turn could mean a smaller operating subsidy payment per vessel. While this proposal might seem revolutionary, it really is no more than a fair and reasonable extension of the principle embodied today in section 911 of the Internal Revenue Code, which exempts income earned abroad by Americans living abroad.

This proposal, while new to the United States, has been used by other maritime nations. Norway, Finland, and Denmark, for example, have special provisions for the tax treatment of merchant seamen. Most recently, the Swedish Shipowners' Association proposed to its government the removal of all income taxes on merchant seamen and officers. We are presently reviewing this proposal with our member companies and with union representatives to ascertain its ultimate workability.

Another area which greatly concerns us relates to vessel construction and conversion for American operators. Last year, Congress responded to the administration's failure to support new construction subsidy funds by granting ODS operators limited authority to have work performed in a foreign shipyard. That authority, however, expires September 30, 1982, unless the Administration requests $100 million in new CDS funds for fiscal year 1983 or presents an alternate shipbuilding program. As we all know, the Administration refuses to do the former, has not yet done the latter, and it seems unlikely it will do so before Congress acts on the fiscal year 1983 budget. Consequently, the foreign building authority will, by its own terms, expire in approximately five months.

We fully support the maintenance of a domestic shipbuilding base for commercial vessel conversion and construction, but we also strongly urge that steps be taken to allow American operators to modernize and expand their fleets pending the development of a U.S. shipbuilding program. American flag operators should not be allowed to become the innocent victims of the administration's budget cutting in the ship construction area. We, therefore, urge this Subcommittee to extend the existing authority for foreign conversion and shipbuilding and we urge that this be done soon—not at the last minute—so that companies can engage in long-range planning.

In a related matter, we urge this Subcommittee to make the Capital Construction Fund available to American operators regardless of where their vessels are built. If such action is not taken our tax law—subpart F—will, because its benefits are available only to foreign flag vessels, encourage the growth of a foreign-flag, rather than an American fleet. This is totally contrary to the Nation's maritime policy as contained in the Merchant Marine Act of 1936 as amended.

We also believe that the money paid back to the Maritime Administration by American operators pursuant to various authorities be considered proprietary funds of the Maritime Administration. Congress originally appropriated such funds for maritime programs; therefore, any of that subsidy money paid back to MarAd should be earmarked for the uses intended by Congress, not mingled with general Treasury receipts.

Such funds include those paid back by operators wishing to place their CDS built vessels in the domestice trades; the proceeds from the sale of reserve fleet vessels; and subsidy monies repaid as a result of an operator's decision to suspend his operating subsidy contract. All should stay with the account of the Maritime Administration.

According to Maritime Administration figures for last 5 fiscal years, MarAd has made payments into the general receipts fund of the U.S. Treasury of approximately $110.5 million from the repayment of CDS. In addition, MarAd has made payments of approximately $13.9 million to the U.S. Treasury from the sale of reserve fleet vessels.

Finally, Mr. Chairman, we believe the Administration's proposed cutback in the title XI mortgage guarantee program for vessel construction should not be adopted. For fiscal year 1983, the Administration wants a limit of $600 million in new loan guarantee commitments, $75 million less than in fiscal year 1982.

The title XI program is vital to the shipbuilding and ship operation industries, especially with respect to domestic trade vessels. We believe the imposition of an annual ceiling on this program will restrict the ability of vessel operators to upgrade and expand their fleets in the United States, and thereby work against national economic and defense objectives.

As this subcommittee knows, title XI guarantees do not involve appropriated funds. It is the cheapest form of government aid. Limiting this program is irrelevant to the effort to balance the Federal budget but does serious mischief to a program that has helped build millions of tons of U.S.-flag shipping.

In conclusion, we greatly appreciate your support for the American merchant marine and we look forward to working with you and your Subcommittee in the months ahead.

STATEMENT OF MATSON NAVIGATION CO.

The Council of American-Flag Ship Operators (CASO) has urged the Subcommittee on Merchant Marine to adopt an amendment to S. 2336 which would, in the absence of construction-differential subsidy [CDS] funds, permit operators receiving operating-differential subsidy to acquire, construct, or reconstruct vessels in foreign shipyards. The proposed amendment would prohibit foreign constructed or reconstructed vessels from engaging in the coastwise or domestic trade except on those voyages specified in the first sentence of section 506 of the Merchant Marine Act, 1936. Section 506 provides that vessels built, reconstructed or reconditioned in the United States with the aid of construction-differential subsidy must be operated exclusively in the foreign trade "* * * or on a voyage in foreign trade on which the vessel may stop at the State of Hawaii, or an island possession or island territory of the United States * * *."

If the vessel makes a such a domestic call, however, section 506 requires a pro rata payback of CDS to the Maritime Administration [MarAd] for the theoretical purpose of equalizing the subsidized vessel's cost with the vessel cost of non-subsidized operators such as Matson Navigation Co. which operates a dedicated service in the domestic U.S. Pacific Coast/Hawaii trade. Section 506 provides that the amount of CDS which must be repaid is 1/25th of a vessel's total CDS multiplied times a fraction whose numerator is the gross revenue derived from the domestic trade during the preceding year and whose denominator is the gross revenue derived from the entire voyages completed during the preceding year.

To our knowledge, the only operator currently using the section 506 procedure is U.S. Lines which operates westbound-only from the U.S. Atlantic and Pacific Coasts to Hawaii. In spite of the inherent advantages section 506 offers to U.S. Lines over Matson and the other non-subsidized operators in the Pacific Coast/Hawaii trade, its application has at least been limited to ships built in the United States.

CASO proposes to extend this domestic trading privilege from U.S. subsidy-built ships to vessels acquired, constructed or reconstructed in foreign shipyards. Section 27 of the Merchant Marine Act of 1920, commonly known as the "Jones Act", and predecessor statutes have excluded foreign built ships from the U.S. domestic trades from the earliest days of the Republic, with very limited exceptions. Virtually every other major maritime nation of the world has long maintained a comparable provision in its statute. Matson currently has invested over $250 million in vessels and equipment purchased in the United States. This investment has been made without Government construction subsidy and Matson, therefore, opposes the ability of its direct competition to use low cost foreign ships.

Exhibit three of the CASO statement makes the allegation that without this amendment, U.S. Lines cannot acquire vessels domestically and remain in the foreign trades due to the high cost of U.S. construction, nor can it acquire foreign vessels without giving up its Hawaii service. Matson submits that if the amendment is not adopted, U.S. Lines is free to dedicate a vessel built in the United States without CDS to its domestic Hawaii service and operate and compete in that trade on the same basis as Matson and the other Jones Act operators have competed in Hawaii's domestic ocean commerce for decades. Moreover, we offer the example of Sea-Land which faced the same issue years ago which U.S. Lines may now face if the construction-differential subsidy program is discontinued. Sea-Land builds unsubsidized ships for the foreign trades in foreign shipyards and operates a fleet of U.S.-built ships in its domestic Alaskan and Puerto Rican services. This option has always been open to U.S. Lines and we suggest that this approach is more desirable than opening the Jones Act trades to foreign-built vessels.

The advantage U.S. Lines seeks is further compounded by the particular characteristics of the Pacific Coast/Hawaii trade. Matson and other Jones Act operators provide a dedicated service to Hawaii, both eastbound and westbound, from the U.S. Pacific Coast in the presence of a very substantial westbound cargo imbalance. Since relatively little cargo moves eastbound from Hawaii to the United States mainland, ships on this segment of the voyage have substantial excess cargo capacity. By contrast, U.S. Lines' foreign service already supports its operation so that U.S. Lines does not have to rely on the relatively small Hawaii trade to maintain its operation, giving it an inherent advantage over smaller domestic operators.

U.S. Lines acknowledges that it is the only U.S. operator utilizing section 506. Matson feels it is eminently reasonable for U.S. Lines to continue using Section 506 until its existing U.S.-built equipment wears out. As that date approaches, U.S. Lines can reconstruct its vessels or build new ships in U.S. shipyards and continue to serve Hawaii's domestic commerce. If U.S. Lines wishes to build in foreign yards, it may operate in the foreign trades on the same basis as other U.S. flag operators. U.S. Lines, however, wants it both ways.

CASO indicates they are very concerned that U.S.-flag operators in the foreign trades achieve operating cost parity with their low cost foreign competitors and rightfully so. CASO should, therefore, be sensitive to Matson's concern that the relatively small repayment provision contemplated by their suggested amendment cannot significantly reduce the inherent U.S. Lines advantage. Two aspects of the suggested CASO amendment are particularly troublesome.

First, at today's vessel cost and high interest rates, it is essential that any premium payment contemplated in return for using foreign ships in the domestic trades require the payment of interest on the entire unamortized amount of CDS equivalent attributable to the Hawaii trade. Section 506 does not currently require the repayment of interest. In 1936, however, the absence of interest payments may not have been a serious problem. This is no longer true today. Assuming that U.S. Lines Hawaii service produces 15 percent of its total trans-Pacific revenue and assuming a $100 million U.S. vessel which can be purchased for $50 million in a foreign shipyard, the foreign-built vessel would have more than a one million dollar cost advantage over the U.S.-built vessel during the first year of operation. This cost advantage arises from the fact that the owner of the U.S.-built vessel must pay interest on the entire vessel cost, less the down payment, while the owner of the foreign-built ships pays interest only on the much smaller debt and no interest at all on the U.S.-foreign cost differential. The attached table sets out the calculations used in arriving at this conclusion.

This existing inequity in section 506 should be corrected. The interim rules promulgated by MarAd for tank vessels, and proposed for all vessels, in cases of total repayment of outstanding CDS and lifting of domestic trading restrictions, require that interest on the unamortized CDS be computed from the day of disbursement of each CDS payment through the day the CDS payment is received. In other words, the Maritime Administration has officially recognized the inequity in permitting refund of CDS without interest.

Yet, the Maritime Administration's interim rule cannot be directly applied here, as the CASO amendment suggests. This rule was not intended to be applicable to the mixed foreign and domestic voyage situation in which the annual payment is only a prorata portion of 1/25th of the United States and foreign cost differential. The rule's application here would have little effect on the cost advantage of U.S. Lines in building or rebuilding vessels in foreign yards.

Since the interim regulation deals with full repayment of unamortized CDS in a lump sum and contemplates a one time interest calculation on the entire amount, this would mean that interest would only be calculated on the amount of CDS equivalent to be repaid in any one year. Rather U.S. Lines should be required to pay interest annually on the full outstanding amount of CDS equivalent allocable to its Hawaii service. The difference for one year is over $1 million, using the same assumptions as above.

Second, CASO proposes that the repayment be calculated using "* * * 50 percent of the cost of an equivalent vessel built in the United States * * *." The problem with using 50 percent of the cost of an equivalent vessel is that, as a practical matter, foreign ship construction can be performed at less than 50 percent of U.S. shipyard costs. If foreign construction costs were 50 percent of equivalent U.S. vessel prices, it would then be appropriate to use 50 percent of the cost of an equivalent U.S.-built vessel to perform the premium payment calculation. But if foreign costs are, for example, only 35 percent of equivalent U.S. vessel shipyard prices, the premium payment calculation should be performed using 65 percent of an equivalent U.S. vessel's shipyard price.

Finally, the administration is working on a maritime policy bill that will address the promotional aspects of U.S. maritime policy. It is inappropriate at this time to make what is an abrupt departure from traditional U.S. maritime policy by allowing foreign constructed or reconstructed vessels into the U.S. domestic trades prior to the consideration of a comprehensive maritime promotional program.

Matson has provided quality ocean shipping service between the west coast and Hawaii for 100 years. This service has been provided with vessels that have been privately financed without the benefit of Government construction or operating subsidy. We urge the members of the Senate Committee on Commerce, Science, and Transportation to reject this amendment and let U.S. Lines compete in Hawaii under the same rules as all other domestic operators—with ships built in the United States.

COST ADVANTAGE OF A TRANSPACIFIC CDS BUILT VESSEL CALLING AT HAWAII OVER A NON-CDS BUILT VESSEL

	Non-CDS vessel		CDS vessel
Cost of vessel	$100,000,000		$100,000,000
		[1] 50,000,000	
Cost to operator	100,000,000		50,000,000
Downpayment	[2] 12,500,000		[3] 12,500,000
Debt	87,500,000		37,500,000
First year interest at 14 percent	12,250,000		5,250,000
Depreciation (1/25 cost)	4,000,000		2,000,000
First year expense for depreciation and interest	16,250,000		7,250,000
Difference in first year expense		9,000,000	
Difference allocable to Hawaii (15 percent)		1,350,000	
Less CDS refund based on Hawaii revenues (15 percent of $2,000,000)		300,000	
First year advantage to CDS built vessel calling at Hawaii		1,050,000	

[1] Less CDS.
[2] 12½ percent.
[3] 25 percent.

Assumption: A U.S.-flag transpacific vessel calls at Hawaii westbound, the Hawaii leg representing 15 percent of its round trip revenues and expenses.

CHERAMIE BROTHERS, INC.,
Golden Meadow, La., April 12, 1982.

Senator SLADE GORTON,
Chairman, Merchant Marine Subcommittee, Committee on Commerce, Science, and Transportation, Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR GORTON: I have read in the recent issue of the Ocean Construction Report dated April 5, 1982 that you will be holding a hearing pertaining to MARAD Authorization Funding on April 17.

My position on Marad Funding is the same as when I wrote to you on February 19, 1981. To be more specific, I oppose this financing more now than I did then. I have had a chance to see for myself, as many others in this area are now seeing, the very critical situation this type of financing created in a little over a period of one year. Exactly what I predicted has come to pass.

For your records, I am enclosing another copy of my letter of February 19, 1981 along with a copy of a letter I sent to Mr. David Stockman on December 23, 1981. I also am enclosing a copy of my response to Mr. Ben Fellows in reference to his letter to me of February 20, 1982.

Again, I wish to state that I would be more than happy to discuss the abuses which I see here in the Gulf of Mexico with regard to the use of Title XI financing.

Sincerely,

MINOR CHERAMIE.

Enclosures.

EXPRESS BOAT CO., INC.,
Golden Meadow, La., February 19, 1981.

Hon. EDMOND D. FITZGERALD,
Director, Office of Ship Financing Guarantees, Department of Commerce, Washington, D.C.

DEAR MR. FITZGERALD: The Charamie Brothers Companies (Express Boat Co., Inc.) operate twenty-nine (29) offshore supply vessels in the Gulf of Mexico in support of drilling and production efforts by our oil companies. Our companies have been doing this since 1947. We have been approved by the Maritime Administration for the purpose of receiving government guarantees under Title XI financing pursuant to the Merchant Marine Act of 1936. We have never availed ourselves of these guarantees; the private sector has been able to meet our financing requirements.

Very recently we have learned that several companies with practically no experience in the business have received government guarantees. In particular, one company has received a guarantee to build thirteen (13) vessels of the supply boat nature. This company has never been in business before and their operating personnel have very little experience. It is a disappointment to us to see substantial competitors come into the business without a background of successful vessel operations. We understand that Title XI is to help those who are established in business and who can demonstrate a history of successful operations but who cannot secure adequate private financing.

It pleases us to see changes in Washington thinking concerning liberal use of federal funds. Those of us who have built substantial businesses in a competitive, free market are happy to see the changes that are being suggested. However, we would like to call to your attention the fact that Title XI is being abused so as to finance large scale ventures without sufficient capitalization and without sufficient experience. The only result of this is that two or three years hence we shall face the break-up of these weak companies. When this happens the entire industry suffers. The private sector is less willing to extend to the substantial operator the credits necessary. We would respectfully request that you undertake to investigate whether or not the Title XI program is presently being utilized to assist those with experience in the business or is being employed as a source of cheap financing for undercapitalized, inexperienced operators.

I shall be more than happy to discuss with any of your representatives the abuses which we see here in the Gulf of Mexico with regard to the use of Title XI financing.

Cordially and sincerely yours,

MINOR J. CHERAMIE.

CHERAMIE BROTHERS, INC.,
Golden Meadow, La., December 23, 1981.

Hon. DAVID A. STOCKMAN,
Director, Office of Management and Budget,
Washington, D.C.

Re: Ocean Construction Report's article on title XI loan guarantees.

DEAR SIR: First of all, my sincere congratulations for the above mentioned article and what it could signify for the future of the boat industry, especially here in South Louisiana.

The exact nature of things to come which I predicted to you in my letter of February 24, 1981 are happening. At this very writing, I can show you at least fifty (50) vessels within a hundred (100) mile radius of my office without any work because of overbuild.

The abuse of title XI monies are presently creating a very serious situation in the boat business. When an operator has his vessels down, he will come down on his prices for his equipment. This causes a chain reaction in that you find yourself working without any margin of profit. The next step, not too far down the line, will eventually mean bankruptcy. When it is all over, neither the operator or the oil companies which usually hires these vessels gain anything. It is simply catastrophe.

Please continue to use the ax as the article states. I believe this is the only remedy left for the legitimate operators to keep on in business.

Sincerely,

MINOR CHERAMIE, Sr.
Vice President.

Enclosure.

OCEAN CONSTRUCTION REPORT,
Houston, Tex., November 30, 1981.

BNOC, CONOCO PLAN NEW PIPELINE SPUR IN NORTHERN NORTH SEA

Since plans for the huge UK gas-gathering pipeline system have fallen through because the British government refused to guarantee financing, British Petroleum, British National Oil Corp. and Conoco have joined for a privately-financed 57-mil. northern line which will tie into the Shell/Esso main FLAGS pipeline system that extends from the Brent field to St. Fergus, Scotland. Final plans for the $192 million project are being drawn up now; contracts setting the project in motion are to be signed in about 3-4 weeks. The line would be built by BNOC with BP as operator. The pipeline would carry slightly less than 100 MMcf/d of gas and come on stream in 1983. The 278-mi. FLAGS system is expected to startup in early 1982, making it the largest offshore gas line in the world. Details on pipeline specifics and when the project will go out for bids should be disclosed soon.

HIGH SEAS SUBSIDE IN NORTH SEA; ACCOMMODATION VESSEL, PLATFORM ADRIFT

A severe storm, packing winds as high as 100-mph and churning waves as high as 50-ft., battered the North Sea last week, setting adrift the semi multipurpose accommodation vessel SEDCO-PHILLIPS SS and Hamilton Borthers' TRANSWORLD 58 converted production platform in the Argyll field. At presstime, the PHILLIPS SS was about 2,100 ft. from the Tor drilling/production platform in the Norwegian sector and was stabilized by a rescue tug. The vessel lost an anchor Nov. 24 and began drifting dangerously close to the Tor. Eighteen men were evacuated from the PHILLIPS SS but as the storm died-down, further evacuation was not required. The TRANSWORLD 58 was set adrift after its 8 anchor cables snapped. Remaining chains were cut free, letting the platform drift toward the Danish Gorm field complex. By mid week, a Hamilton Brothers spokesman said 5 support vessels were expected to get a line on the platform anytime. A portion of the crew of the Argyll platform was airlifted to Stavanger. No injuries were reported in either incident. Two other production platforms—the Ekofisk 20-C and Eldfisk 2-7B—suffered some minor damage and were shut down.

TITLE XI LOAN GUARANTEES DRY UP

The Office of Management and Budget (OMB) ax has fallen on the Maritime administration's Title XI loan guarantee program for offshore rigs; OMB is proposing eliminating such funding for workboats. Title XI funding was cut as part of the Reagan Administration's budget cutbacks because the OMB considered the guarantees a direct subsidy to oil companies, among other factors. Currently, about 50 rigs are on MARAD's list of active pending applications for Title XI funding. About 70 workboat applications are pending. The MARAD loan guarantees run about 3 points below the prime rate with a payback period of 15 years of rigs. Alternative financing will be as much as 6 points higher interest and a payback period of 5-9 years.

BRAZIL MAY HAVE NEW LARGE FIELD

Brazil's Petrobras believes a significant strike in the Campos Basin may be a new field separate from other structures discovered in the area thus far. Initial tests yielded 1,600 b/d of high quality light crude at depths of around 8,300-ft. Petrobras officials report that ultimately the new field could reach daily production as high as 12,000 b/d; field reserves could range from an estimated 25 million to 30 million barrels.

BPTS TO PROCEED WITH DEVELOPMENT OF ULA FIELD

BP is now finalizing its development plans for the Ula field, located in Block 7/12 in the Norwegian sector. BP's timetable calls for Ula's revised development scheme to be presented.

CHERAMIE BROTHERS, INC.,
Golden, Meadow, La., March 17, 1982.

Mr. BEN FELLOWS,
President, Committee for Title XI Vessel Financing,
Washington, D.C.

DEAR SIR: This is to acknowledge receipt of your letter to me dated February 20. To answer your first two questions in this letter, the following are my answers: (1) Title XI Vessel Financing is not important to my business; (2) I am extremely willing to see it die.

I have carefully considered your request for a contribution in support of said Title XI Vessel Financing Guarantee Program and to me this programs practical aspects are not appealing, and never have been.

To be more specific, I am enclosing for your files a letter I have sent several months ago to Mr. David Stockman, along with copies to our Louisiana Delegation.

Sincerely,

MINOR CHERAMIE,
Vice President and Chief Executive Officer.

COMMITTEE FOR TITLE XI VESSEL FINANCING,
Washington, D.C., February 20, 1982.

Mr. MINOR CHERAMIE:
Cheramie Bros. Boat Co., Inc.,
Golden Meadow, La. 70357

DEAR MR. CHERAMIE: How important is the Title XI Vessel Financing Guarantee Program to your business? Are you willing to see it die?

As you probably know, there is only a little over $1 billion guarantee authority left—against which over $2.5 billion in feasible applications are pending. Unless Congress expands the program, it will just wind down . . . which is apparently the goal of the Office of Management and Budget. Last year, for the first time in history (and with no statutory basis), OMB unilaterally imposed a ceiling of $1,050 million on Title XI's guarantee authority, and subsequently reduced the ceiling to $675 million in fiscal year 1982 and $600 million for fiscal year 1983.

To forestall Title XI's demise, a group from various segments of the maritime industry organized the Committee for Title XI Vessel Financing and put up the seed money to get it going. To date we have accomplished the following:

Formally established a non-profit corporation to conduct the Committee's business and shield members from any liability;

Commissioned an Economic Impact Study of the Title XI Program (the most comprehensive and authoritative analysis yet) by Temple, Barker & Sloane of Lexington, Massachusetts which shows the generation of 1,190,000 man years of employment, an average of 99,000 jobs annually, and that the OMB restrictions threaten 135,000 jobs and $8.9 billion to the economy;

Engaged consultants and counsel to brief (so far) the staffs of both Merchant Marine subcommittees and personal aides of 28 key members of Congress in both chambers;

Testified February 11 before the Senate Budget Committee's Federal Credit Task Forces to demonstrate Title XI has no budget impact and does not "crowd out" capital investment borrowers from the bond markets;

Preparing testimony on Title XI for upcoming Congressional hearings;

Drafted bill to increase Title XI's present guarantee authority by $3 billion without unilateral ceilings by OMB. This bill will hopefully be introduced in both chambers sometime next month;

Begun a bi-monthly newsletter and obtained coverage in the Journal of Commerce to keep the industry posted on our activities.

All this costs money, naturally . . . and our "seed" funds are nearing depletion, just as we are beginning to make an impact. To maintain the momentum we have built up on Capitol Hill we need help . . . yours:

(1) A one-time contribution of $2,500. This is a self-destruct operation that will detonate when its mission is accomplished, presumably sometime this year.

(2) An expression of your willingness to contact in writing or in person Members of Congress when asked by the Committee at critical "gateways" in the legislative thickets.

Enclosed is a summary "About the Committee," a fact sheet on Title XI and an application for membership. Feel free to make Xerox copies and send to others whom you feel should join in the common effort to save Title XI for all segments of the industry. If you have any questions, please call the Committee's Secretary, Tom Mills at 202/737-6909.

Without more industry support, the Committee and the Title XI program will sink. It's that simple.

Sincerely yours,

Ben E. Fellows,
President.

Joint Maritime Congress,
Washington, D.C., April 20, 1982.

Hon. Slade Gorton,
Chairman, Subcommittee on the Merchant Marine, Senate Commerce, Science, and Transportation Committee, Russell Senate Office Building, Washington, D.C.

Dear Senator Gorton: The Joint Maritime Congress appreciates the opportunity to present our views on the Maritime Administration authorizations for fiscal year 1983 through the submission of this statement and enclosed maritime policy paper to be included in the record of the hearings.

As an association of American-owned, U.S.-flag ship operating companies engaged in nearly every aspect of deep-sea commercial maritime service, the Joint Maritime Congress has supported federal programs designed to sustain and fortify the troubled U.S. merchant fleet. We are, however, painfully aware of current economic conditions and recognize that fiscal austerity is a prerequisite to rejuvenating the nation's economy. Even more important, we, along with others, are eagerly awaiting the Administration's maritime program. Consequently, we view the current MarAd authorizations as a "stop gap" measure until this program is announced and put into place.

In that context, we are in agreement with the funding levels authorized by your bill, S. 2336, which essentially places maritime programs on hold pending a clear signal on our national maritime policy from the Administration. We would, however, like to address several critical issues: the Operating Differential Subsidy Program (ODS), the Title XI Federal Ship Financing Program, and foreign construction of U.S.-flag subsidized vessels.

The $454,010,000 proposed by both the Administration and you for fiscal year 1983 Operating Differential Subsidy outlays will sustain the program at its current level. That level enables the operators of 151 vessels, 128 liners and 23 bulkers, to achieve cost parity with their foreign competitors. That these vessels remain operational is of the utmost importance since 124 of the 151 are ships of the greatest military utility, (3 Roll-On/Roll-Off vessels, 15 nonjumbo tankers, 4 refrigerated cargo ships, 48 partial container ships, and 54 break bulk vessels). These ships make a significant contribution to the United States' military sealift capability. In addition to the question of the military value of these vessels, we believe strongly that any action that would further deplete the U.S. merchant fleet's commercial strength and size would be highly undesirable. As you know, today, even with the subsidy program, the U.S.-flag merchant fleet carries but 3.6 percent of our entire oceanborne foreign trade and less than two percent of essential strategic minerals.

We are pleased that the Administration and this Subcommittee are cognizant of this program's worthiness and hope to maintain it at its current level through the next fiscal year. Currently, it is the policy of the Office of Management and Budget not to accept any new ODS contracts even if vessel lay-ups, sales or charters to the military Sealift Command make additional funds available. For the time being, in view of the present budgetary crunch, this may be a rational policy. However, it is a policy that if continued would lead to the gradual diminution of the U.S.-flag subsidized fleet.

Subsidized vessel operators, required to replace overage ships, are doing so on the basis of one new vessel for every three or four old vessels. Greater efficiency in cargo design, vessel size and speed explain the fact that one new modernized vessel can transport the same cargo in the same time as three or four older vessels. If new ODS contracts are not entered into in the future, clearly the real expense, while not necessarily the absolute expense, of the program will decline. Although OMB and the Treasury may find that prospect appealing, it will eventually result in a U.S.-flag subsidized fleet, one-quarter to one-third the size it is today.

Barring the implementation of practical and effective alternatives, new operators would be undeniably shut out from entering the foreign trades. In the interest of preserving and strengthening our merchant fleet, the Joint Maritime Congress strongly believes that an ongoing policy of refusing new ODS contracts without devising workable alternatives is unwise and not in our Nation's best economic and security interests.

This conviction has prompted the Joint Maritime Congress to formulate a series of recommendations which have been submitted to the Reagan Administration and are included with this statement. These recommendations would strengthen the U.S.-flag fleet, and we respectfully urge the Secretary of Transportation that they be part of a maritime program.

The second critical issue concerns the Administration's recommendation to reduce the fiscal year 1983 ceiling on title XI loans from the fiscal year 1982 level of $1.6 billion, recently approved in the December continuing appropriations measure, to a mere $600 million. This self-sustaining and highly successful maritime program has assisted in the construction of more than 7,000 vessels over the course of its history. The program generates a yearly income through guarantee fees and investigation charges paid to MarAd by title XI applicants and recipients. That annual income approximates $50 million—$46 to $48 million of which goes into a revolving fund. All defaults (there have been only 11 throughout the program's 44-year life) have been absorbed in their entirety by the fund, and annual loan repayment, averaging $400 million, reduces the level of government-guaranteed debt. Furthermore, since its inception, the title XI program has cost the Federal Government only $0.8 billion, less than any other Federal Guarantee Program. Although S. 2336 proposes a somewhat higher ceiling of $675 million, the difference would not impact significantly on vessel construction.

In light of these facts, we believe that a $600 or $675 million ceiling on Title XI loan guarantees is unreasonably low. We do not see the logic behind crippling a fruitful program which does not require the outlay of a single dollar. None of the Administration's charges against federal credit programs—the high administrative costs, distortions of the private capital market and the view that these programs become deferred subsidies once defaults occur—applies to the Title XI program for all the reasons just mentioned.

Erosion of the Title XI program will debilitate U.S. shipbuilding capability, and result in reduced domestic economic activity, through job and revenue losses. The Committee for Title XI Vessel Financing estimates that in 1980 the program generated 37,000 jobs and a $4.8 billion stimulus to our nation's economy. Additionally, our national security will be threatened with the dilution of the Title XI program, because this program is a proven stronghold for maintaining a shipbuilding and supplier base essential for the construction of vessels that are available as naval auxiliaries in time of war or national emergency.

Because MarAd now holds approximately $2.5 billion in Title XI applications and only $1.4 billion of the $9.7 billion statutory limit remains unobligated, we advocate not only the continuation of ceiling levels at least at the fiscal year 1982 level, but an increase of the current $12 billion statutory limit to $15 billion. Further, those additional loan guarantees should be made available solely for the construction of merchant vessels equipped with national defense features. Our economic and defense postures stand to gain while no one loses. When the taxpayer is not having to contribute a single dollar toward a flourishing program responsible for stimulating our economy and improving our defense readiness, today the Administration's and the nation's two foremost concerns, what is the rationale for chipping away at that program? The Joint Maritime Congress claims there is none.

Finally, we concur fully with the provision in your bill authorizing permanent authority to U.S.-flag subsidized vessel operators for the foreign construction or repair of their vessels. We do feel, however, that tax-deferred capital construction fund monies should not be precluded from use for foreign construction. Without construction differential subsidy and until some degree of parity is achieved between construction costs in the United States and foreign shipyards, those funds, $444,243,495 as of September 8, 1981, will remain untouched. What, then, would motivate a U.S.-flag steamship operator to build a vessel domestically?

Mr. Chairman, we appreciate this occasion to express our views on the authorized levels of fiscal year 1983 funding for the Maritime Administration to the Subcommittee and for the public record. We look forward to continuing our work with you and the entire Merchant Marine Committee to improve the U.S. merchant fleet.

Respectfully,

David A. Leff,
Executive Director.

Enclosure.

Rebuilding the U.S.-Flag Merchant Marine

EXECUTIVE SUMMARY

America's merchant marine is an essential investment in national security and economic strength. This paper discusses the basic problems and realities confronting the U.S.-flag merchant marine today as well as the opportunities presented by world shipping trends and the realization by this Administration of the necessity for a stronger U.S.-flag merchant marine.

It advocates a series of manageable, economically sensible, and militarily important actions that can be taken to bolster the U.S. merchant marine and with it our nation's security. Some of these actions are the responsibility of the maritime industry; others are tasks that only the government can effect. These actions encompass a broad range of issues:

Cargo.—A policy that guarantees a fair share of cargo to U.S.-flag vessls through a series of bilateral maritime agreements with our trading partners and ensures an adequate and steady supply of strategic minerals. The policy should also reaffirm the viability and importance of the Jones Act and guarantee U.S.-flag participation in U.S. coal exports;

Reflagging.—A policy that encourages re-flagging of foreign ships under the U.S. flag through measures such as repeal of the Subpart F exclusion of the Internal Revenue Code and regulatory reform, combined with waivers of certain Coast Guard vessel standards in order to increase significantly and quickly the number of U.S.-flag vessels and take advantage of the current world overtonnage situation;

Investment.—A policy that encourages increased foreign and domestic investment in the U.S.-flag merchant marine through bilateral cargo sharing agreements, legislation that would permit increased foreign ownership and managerial control of domestic corporations, permission—for an unlimited period—for ship operators receiving ship-operating subsidies to construct and repair vessels abroad, continuance of Title XI mortgage loan guarantees at least at current levels, and creation of tax-exempt shipping bonds targeted on building a special class of national defense merchant vessels;

Tax Policy.—A policy that assists operators and encourages investors through repeal of the Subpart F exclusion of the Internal Revenue Code, accelerated depreciation of shipping capital equipment from five years to one year, incentives for shippers to use U.S.-flag ships and income tax reductions, combined with pension assistance, for merchant seamen to lower operating costs;

Regulatory Reform.—A policy that incorporates passage of the Shipping Act of 1981, sponsored by Senator Slade Gorton (R-WA), and maintains mandatory rate filing by shippers with the Federal Maritime Commission, to assist the U.S.-flag fleet in competing effectively and on equal terms with the fleets of other nations;

Subsidies.—A policy that preserves existing operating and construction subsidies until, at a minimum, effective and workable alternatives can be found and put into place;

Civil/Military Cooperation.—A policy that encourages increased civil/military cooperation so that each sector supports the other with measures such as civilian manning of logistic and other Naval support ships, incorporation of merchant ship enhancement and defense features, and construction of a fleet of militarily useful cargo ships financed largely by the government but operated commercially by the private sector in peacetime; and

Improved Efficiency.—Both labor and management must take actions to improve productivity and operating efficiency in order to enable the U.S.-flag fleet to compete successfully with foreign fleets.

This paper recommends that these actions be presented as part of a clear, cohesive policy, announced in a Presidential declaration. Taken together, these actions will help rebuild the U.S.-flag merchant marine and provide our fleet the support it needs to compete successfully against the fleets of other nations and be an effective and reliable supplier of sealift for our national security.

JANUARY 19, 1982.

REBUILDING THE U.S.-FLAG MERCHANT MARINE

America's merchant marine is an essential investment in national security and economic strength. A strong merchant marine enables us to project military force when and where we want it, with strength and staying power. As Admiral Hayward declared in March 1981: "Without adequate and reliable sealift, literally none of our military plans is executable." This investment creates economic dividends as well. A U.S.-flag merchant marine provides an economic alternative to foreign-flag fleets as we enter a decade marked by weakening alliances and rapidly growing national control and support of merchant fleets. It assists our national economy in marketing American products and services abroad, strengthening not hemorrhaging our balance of payments. It creates jobs at home, not just in port cities, but in supporting industries in every state. And a U.S.-flag merchant marine can help guarantee the flow of essential raw materials, vital for our defense as well as our economy.

Rebuilding our merchant marine must be made with an appreciation for the basic problems and realities we face:

First, where we stand today. In 1981, the U.S.-flag merchant fleet carried only 3.6 percent of our foreign trade and less than 2 percent of essential imported strategic minerals. Our dry bulk fleet numbers only 18 ships, many of which are of advanced age. Indeed, the entire U.S.-flag fleet averages 17 years of age, the most elderly of the world's major fleets, a factor which accentuates our difficulties as these ships use more fuel and require larger crews. In addition, today only 20 percent of world trade is with the United States. We cannot enforce principles of free trade and open competition as we could three decades ago when the figure was 50 percent.

Second, the need for a fleet *in-being*. In World War II, we had time to construct merchant marine sealift capacity. No leader, military or civilian, believes that a future conflict will provide us with the same opportunity.

Third, the lack of sheer numbers of merchant ships. In 1950, there were 1,087 privately-owned U.S.-flag merchant ships; in 1981, only 577. During a major conventional conflict, the Soviet Union could field literally hundreds of submarines, a threat far larger and far more capable than the German submarine threat in World War II. Our merchant fleet losses could be staggering.

Fourth, the enormous increase in individual ship carrying capacity. Although this phenomenon works for us economically in peacetime, it would work against us in war. With fewer but larger ships, a single enemy torpedo today could deprive us of five to twenty times the cargo carrying capability that an enemy torpedo could in World War II.

Fifth, the lack of ships suited to our potential military requirements. The economics of modern oceangoing trade have gradually produced fleets of ships that are, in substantial measure, ill-suited to such requirements. Jumbo tankers and large non-self-sustaining container ships are not quickly adaptable to military needs. The Soviet Union has been careful to avoid this problem. They have, for example, some 1,700 break-bulk cargo ships; we have approximately 300, a figure that is attained only by including World War II vessels held in government storage.

Sixth, the decline of our oceangoing merchant marine work force. In 1967, there were nearly 60,000 oceangoing shipboard jobs; in 1981, less than 20,000, and this work force is aging. If we do not create new seafaring jobs *now* to attract young personnel to a career at sea, we will not have the seasoned, experienced work force we will need in the future.

Seventh, the dependence of the United States and its Allies on imported raw materials and thus on seaborne foreign trade. In fact, we and our Allies are even more dependent than we were at the time of World War II. The effective denial of foreign trade would dramatically shake our economy and our defense industry; it would be even more catastrophic to our Allies.

Eighth, international instability. Friendships and alliances today are shaky at best, a point that the Allied response to events in Poland, Afghanistan, and Iran has emphasized with clarity. We cannot automatically count on ships and crews not under direct U.S. control. And the pace and destructiveness of future conflict is likely to be such that we will not have the time or capability to divert the U.S. Navy to seizing U.S.-owned ships registered in other nations or to wait for days or weeks while diplomatic processes attempt to produce the results we need. In situations short of conflict involving our forces, the prognosis is no more encouraging, for in today's world of new centers of economic and political strength, we will control with certainty only the power under our control. During the 1973 Arab-Israeli war, for example, Liberia forbade its ships to carry arms to Israel, notwithstanding the American ownership of these ships and the long-standing cultural and historical ties between Liberia and the United States.

Despite these adversities, there are opportunities as well. The Reagan Administration is committed to maintaining a strong Navy and merchant marine and has put in the Departments of Defense and Transportation the leadership necessary to achieve these objectives. It is also determined to eliminate unnecessary and burdensome regulations, a commitment that is essential if our merchant marine is to compete effectively in the world market. American labor has already indicated that it is willing to operate with the flexibility and innovation that worldwide shipping competition demands today. The coal trade is about to produce a major boost to America's exports and with it a major opportunity for American ships to carry America's trade. Because of our nation's need to import strategic minerals, crucial to our defense industry, many Americans are realizing now that we must guarantee adequate supplies of these minerals, the transportation of which will be entirely U.S.-directed and controlled. Excess ship tonnage on the world market will offer for at least several years the opportunity to bring new foreign-built ships under the American flag at favorable rates. And there is a global trend toward increased cargo sharing among nations either through the multilateral mechanism of UNCTAD or through bilateral agreements. For the United States, this trend holds particular promise, because we carry so little of our massive world trade and because it addresses the essential prerequisite of a successful commercial merchant marine—cargo to carry.

We believe that there are manageable, economically sensible, and militarily important actions that can be taken to bolster our U.S. merchant marine and with it our nation's security. Some are the responsibility of the maritime industry; others are tasks that only the government can effect. Taken together, these actions will help rebuild the U.S.-flag merchant marine and provide our fleet the support it needs to compete successfully against the fleets of other nations.

These actions must be presented as part of a clear, coherent policy to rebuild the U.S. merchant marine, for they are interrelated and their effect will be dissipated if they are introduced piecemeal. Linked in a Presidential declaration, they would signal to investors at home and abroad a long-term consistent climate as well as the conditions of maritime support. A Presidential declaration would also send a necessarty signal to the government itself. Too often, efforts to strengthen our merchant marine have been weakened as governmental departments exchange concessions on maritime issues by our nation for concessions on trade and diplomatic issues by other nations. Even policy decisions established by law, such as government cargo allocation, have been circumvented by the very agencies to which they apply.

This declaration should establish broad guidelines:

The importance of having cargo to carry, which we believe is the single most important step toward a stronger merchant marine. If the cargo exists (whether by mandate or simply encouragement), ships will be there to carry it;

The need to emphasize re-flagging of foreign-built ships as the only way the United States can substantially increase its merchant fleet in an acceptable time period. Emphasis on re-flagging as a near-term action would take advantage of the current and projected excess tonnage available on the world market;

The importance of seeking alternatives to existing construciton and operating differential subsidy programs while maintaining these subsidies until practical and effective alternatives can be put in place. The U.S. maritime industry has declined despite decades of subsidies but few would argue that the United States would even have a base upon which to rebuild if these aids did not exist;

The need to make certain that promotion of shipbuilding does not operate to the detriment of ship operating. Except for fiscal year 1982, U.S.-flag ship operators receiving operating subsidies have been required to buy vessels constructed in the United States, greatly adding to their financial burden. Each industry needs to be strengthened but neither is in such condition that it can afford to support the other;

The military requirement for a U.S.-flag merchant marine under direct American control, and the civil/military partnership that is an essential ingredient of a militarily relevant merchant fleet;

The role of the U.S.-flag merchant marine in an aggressive global American economic policy that emphasizes reciprocity. The United States is still the largest single trading nation. It is time to use the leverage this provides to strengthen our merchant marine and ensure, at least, that it is able to operate with the same support and access the other nations provide their fleets.

These guidelines should be reinforced by specific proposals. The following eight areas for action contain measures that we believe are necessary to rebuild the U.S.-flag merchant marine.

CARGO

Measures to increase the amount of cargo carried in U.S.-flag ships must begin with a clarification and reemphasis of the application of existing cargo reservation measures such as the Cargo Preference Act of 1954 (PL 664). This act mandates that U.S.-flag commercial ships carry at least 50 percent of government-generated cargoes by tonnage. A Presidential proclamation should declare that this act and other cargo reservation measures be strictly adhered to by government agencies, subject only to waivers granted by the Maritime Administration, and the 50 percent figure in PL 664 be treated as a minimum—conforming to the original intent of the law.

Existing cargo reservation measures are, however, inadequate. Furthermore, their beneficial effects are about to be severely eclipsed by the immiment entry into force of the UNCTAD Code of Conduct for Liner Conferences, which is only the most visible manifestation of the growing trend toward multilateral and bilateral cargo sharing agreements. It is particularly important that the Administration decide soon between the multilateral UNCTAD regime, accompanied by appropriate reservations if required, and an extensive regime of bilateral cargo sharing agreements. The worst of all worlds will be to hesitate, for the entry into force of UNCTAD will result in the flooding of U.S. trade routes with ships excluded elsewhere.

Although adoption of the UNCTAD Code would reserve 40 percent of our trade for U.S.-flag ships, we recommend that the Administration pursue a policy of bilateral maritime agreements with provisions for cargo sharing. Adoption of the UNCTAD Code would subject the process of cargo promotion and sharing to a lengthy and potentially fruitless ratification process as well as require a wholesale revision of U.S. shipping and antitrust laws. A policy of bilateral maritime agreements, which the President supported during his 1980 campaign, could be accomplished without legislation, and their use would preserve an essential element of flexibility, being far simpler to revise than the complex multilateral UNCTAD code.

This recommended shift from "free trade" toward bilateral cargo sharing agreements would take advantage of—rather than merely attempt to postpone—the inevitable. These types of agreements have already worked successfully in our trade with several foreign nations. There is no evidence that freight rates have increased out of the ordinary in these trades nor has the quality of service declined since they have been in effect.

These bilateral agreements should be negotiated with a maritime official as the chief negotiator. This would force concentration of emphasis on the maritime interest in these negotiations, an interest that too often has been sacrificed to the interests of other government agencies.

Bilateral agreements would permit rationalization of our maritime trade, eliminating overtonnaging, which has itself lessened the revenues of U.S.-flag companies through unfair competitive practices engaged in by our shipping competitors. The greater revenues that this would provide could reduce the direct subsidies required by U.S. lines. Some bilateral agreements could have an important impact on our defense capabilities. For example, requiring that U.S.-flag ships carry a certain percentage of automobile imports from Japan would promote a buildup in RO/RO ships which are militarily very useful and in short supply in our fleet.

The United States, along with nearly every other maritime nation, has promoted its merchant marie fleet through cabotage restrictions, which have operated primarily to restrict the carriage of trade between domestic ports to the national flag fleet of the country in question. For the United States, this restriction is embodied in the Jones Act, which has been an important source of cargo, particularly for the U.S. tanker fleet carrying Alaskan North Slope oil. This act is an essential element of support for the U.S. merchant fleet. It was reaffirmed by President Reagan during the campaign and should be reaffirmed in any formulation of maritime policy.

There are other measures that can be taken to increase cargo available to U.S.-flag ships. One would be to take advantage of the growing U.S. exports of coal, a commodity which has enormous potential to give the United States shipping leverage because of our extensive and reliable supply. Currently before the House in H.R. 4627, a bill that addresses problems raised by the potential coal export boom and the consequent need to deepen and maintain U.S. ports. An amendmment to this bill by Representative Gene Snyder (R-KY) would guarantee U.S.-flag carriage of up to 40 percent of our dry bulk trade, to be phased in over ten years. Adoption of this measure, the costs of which could be spread over all coal exports and linked to series production of a modern class of efficient coal-powered coal-carrying ships, would substantially increase our dry bulk capacity without removing the financial competitiveness of the coal exports themselves.

A second additional measure to increase cargo would be to provide incentives through the tax system to U.S. shippers who ship on U.S.-flag ships. Today, many American shippers do not support the flag even in cases where the freight rates are equal. Although the Domestic International Sales Corporation (DISC) mechanism, which supports shipping on U.S.-flag vessels has been criticized at home and abroad, we believe that a mechanism, however designed, to encourage exporters to use the U.S.-flag should be promoted as part of an overall policy that aggressively supports our nation's exports and U.S. transportation to carry them. The cost of incentives to send cargo on U.S.-flag ships would be largely offset by reductions in subsidies needed, by increase taxes paid by ship-owning companies, and by improved U.S. balance of payments. The outflow for shipping services alone in 1979 has been estimated to be $4 billion. Such a program could also work to expand exports of U.S. goods and services through promotion of inter-modalism. Such promotions should be part of an overall, global U.S. policy to advance its trade. Other trading nations such as Japan have aggressively marshalled their national assets to promote trade. We must as well.

A third cargo measures concerns strategic minerals. Although study after study has outlined the severe consequences that could ensue if the U.S. supply of imported strategic minerals were interrupted, one key component of our dependence on imported strategic minerals often has been overlooked—less than 2 percent of these minerals arrive in U.S.-flag ships. Even groups traditionally opposed to cargo allocation, such as the National Association of Manufacturers, now recognize that this is a significant problem. Most of our strategic mineral imports are carried on flag-of-convenience vessels that could be denied us in some future crisis whether these vessels are American-owned or not, for the country of *registry*, under international law, has the right—in case of national emergency—to appropriate for its own purposes ships registered under its flag. Also, the particular citizenship of the crew on these foreign-registered vessels may raise loyalty questions in the event of conflict, or even in political crises with other nations. Elsewhere in this paper, we recommend tax and other incentives to encourage the construction of U.S.-flag vessels that could carry these minerals, but the most important incentive would be guaranteed cargo to carry. We believe this incentive would be best achieved with bilateral agreements—similar to those discussed above concerning coal—with countries that are sourcs of the minerals. The goal would be to have U.S. carriage of at least 40 percent of our strategic minerals trade. The pace with which we attain this goal would depend on the speed with which the U.S. bulk fleet can be built up through re-flagging or construction of new ships in America or abroad.

REFLAGGING

Reflagging of ships now operating under flags of other nations is the only way, short of a World War II-type crash construction program, that America can significantly increase the numbers of U.S.-flag vessels in the next decade. The cargo policy discussed above, therefore, must be accompanied by measures targeted to produce reflagging.

Many of these measures are discussed in other sections of this paper. They include repeal of the Subpart F exclusion of the Internal Revenue Code (see page 10), and regulatory reform (see page 11). In addition to these measures, the Coast Guard would have to grant exceptions from certain vessel standards which would be prohibitively expensive and perhaps impossible for many foreign vessels to attain. There is already precedent for the Coast Guard to waive its standards, as recently in the case of Consolidated Carribean Transport, to allow foreign vessels to be documented under the U.S. flag. Documentation for these reflagged vessels could, instead, be tied to their meeting the standards of the international ship classification societies, such as Lloyd's of London, and the waiver of Coast Guard standards could also be applied only to existing vessels re-flagged while the new U.S. fleet is built up at home and abroad.

INVESTMENT

Rebuilding the U.S.-flag merchant marine will dictate a major increase in capital investment. The declaration of a national merchant marine policy and the guaranteeing of cargo opportunities through bilateral cargo sharing agreements as well as cargo promotion incentives would make a major contribution toward investment in the U.S. merchant marine by providing the necessary promise of long-term stability and markets. These measures should, however, be part of a comprehensive, targeted set of measures to stimulate both domestic and foreign investment.

Although most of the measures listed below would encourage both foreign and domestic investors, one legal change is required specifically to attract foreign investment. Following existing U.S. laws, the Coast Guard will not document a vessel under the U.S.-flag unless the owner is a U.S. citizen or, with very limited exception, in the case of corporations, the controlling interest in the corporation is owned by U.S. citizens. Legislation should be sought to permit increased foreign ownership of domestic corporations, with the foreign owners allowed direct managerial control. Furthermore, in the case of documentation questions, the Maritime Administration, not the Coast Guard, should be the final determiner as to whether a vessel's ownership is in compliance with U.S. statutes. The current international climate, combined with the other incentives listed in this paper, is such that there is substantial potential to attract foreign capital seeking a stable home. Allowing foreign owners direct managerial control would be a major alteration of policy. It would, however, increase the attraction to foreigners of investment in the U.S. flag, and it would provide an important influx of managerial talent and innovation.

Because Construction-Differential Subsidy (CDS) funds have been virtually eliminated during fiscal year 1982, U.S.-flag ship operators, receiving operating subsidies (and access to government cargoes) and therefore committed by law to replace these subsidized ships with U.S.-built tonnage, have been permitted for this year only to construct replacement vessels abroad. However, most subsidized ships are due for replacement in later years. Furthermore, only a major and unlikely increase in construction subsidies could handle a build-up of the U.S.-flag fleet beyond its present capacity. We recommend, therefore, that operators receiving operating subsidies be permitted to construct and repair vessels abroad for an unlimited period. Operators taking advantage of this change would also be permitted to use Capital Construction Fund (CCF) deposits for foreign construction. To ensure that other desired U.S. maritime objectives are met, operators exercising the option to build abroad would, in addition to receiving U.S.-flag privileges, have to comply with Coast Guard regulations and be available to serve in the Department of Defense's Sealift Readiness Program, as well as be restricted from operating in the U.S. domestic trade.

The permission to build ships abroad has already been criticized widely by the U.S. shipbuilding industry, which by all accounts is in serious condition, a condition for which increased Navy building is an inadequate solution. To help remedy this condition in an industry that is also essential to the national security of the United States and the economic health of many states, we recommend two measures that can assist investment in both the shipping and the shipbuilding industries without forcing either to bear the burdens of the other.

The first is to continue Title XI mortgage loan guarantees for construction of ships in U.S. yards. A $1.6 billion ceiling has been authorized for fiscal year 1982, the same as for fiscal year 1981; however, there are indications that guarantees granted in actuality will fall far short of this level. In view of the fact that these guarantees are guarantees and not expenditures of scarce funds (the program actually makes money and defaults have numbered only eleven in the entire history of the program), loan guarantees should be treated as an aggressive tool to attract new capital; they should not be deemphasized or preserved in name but emasculated in practice.

The second measure that can assist investment in both industries would be to create a series of tax exempt shipping bonds, guaranteed by the government, aimed at small as well as large investors, and targeted on a special class of national defense merchant vessels (see page 14 of this paper). Such bonds in addition to directing small investors toward a particular national need would also be good public relations—publicizing the U.S. merchant marine and providing a sense of personal participation in a tangible investment for our nation's security.

TAX POLICY

The creation of tax exempt shipping bonds is just one way in which tax policy can be used to stimulate investment and assist both the ship-operating and shipbuilding industries. We recommend several additional measures.

The first and most important would be the repeal of the Subpart F exclusion of the Internal Revenue Code which permits U.S. corporations to escape taxes on earnings (hence reducing revenues to the U.S. Treasury) from foreign shipping operations if these profits are re-invested in shipping operations abroad. The same earnings are taxed when used to build ships in the United States. Repeal of the Subpart F exclusion should be accompanied by permission for these same corporations to invest earnings, tax deferred, in the Capital Construction Fund for the construction of U.S.-built ships. The benefit of this repeal could be extended directly to the ship-operating industry by allowing that a certain portion (perhaps one half) of the income from foreign shipping operations could be deposited, tax deferred as well, into a fund for the purchase of foreign-built ships that would, however, have to be operated under the American flag.

The second additional measure would be to accelerate depreciation of shipping capital equipment. The Economic Recovery Tax Act of 1981 reduced depreciation time from fourteen and one-half to five years. Accelerating depreciation from five years to one year would assist ship financing, and it could be conditioned with a "buy American" provision to help ship construction in the United States.

A third recommended measure in the area of tax policy—incentives for shippers to use U.S.-flag ships (*e.g.*, investment tax credits)—already been discussed under "cargo" (page 7).

A fourth measure consists of income tax reductions combined with pension assistance for merchant seamen. Income tax reductions are already in practice in Norway, lowering operators' costs by reducing the wages necessary to pay merchant seamen. The result of tax reductions combined with pension assistance would be that the U.S.-flag fleet would be more competitive with those of other nations. The benefits would accrue to non-subsidized as well as subsidized operators. The tax portion of this measure would be relatively simple to implement by taking advantage of a change in Section 911 of the IRS Code incorporated in the tax reforms of 1981 which exempts the first $75,000 of income for Americans working abroad. It would apply to seamen serving on oceangoing vessels of 1,000 gross registered tons or more. In view of the fact that ameliorating the income differential between seamen on U.S. and foreign-flag ships accounts for most of the operating subsidies, this exemption could help pay for itself by reducing the amount expended on direct operating subsidies. The pension assistance portion of this measure would be required because pensions would be lowered as wages are lowered. It could be linked to participation in the U.S. Navy's active reserve, helping to increase the mobilization potential of U.S. forces while lowering costs for operators in peacetime.

REGULATORY REFORM

The U.S.-flag merchant marine has been hamstrung by burdensome regulations that have hindered efficiency and made these carriers less competitive with foreign fleets. This area needs little amplification since important and highly beneficial regulatory reforms have been incorporated in the Shipping Act of 1981, sponsored by Senator Slade Gorton (R-WA). On December 31, 1981, Transportation Secretary Drew Lewis indicated publicly that the Reagan Administration supports the reforms in this bill in principle and in most of their details, although not in one important respect—the retention of the requirement for shippers to file their rates with the Federal Maritime Commission.

We believe passage of the Gorton Bill should be a part of any national policy to rebuild the U.S.-flag merchant marine. It would reduce uncertainty for operators and investors alike and increase the U.S. fleet's ability to compete. Rate filing, which protects shippers, ship operators, and consumers, should be retained. It is the effective method of enforcing anti-rebating statutes and protecting U.S.-flag carriers from unfair competition by foreign carriers, and it protects manufacturers from discrimination as regards size by all carriers.

SUBSIDIES

In the course of this paper, we have outlined a series of measures that are important building blocks for a revitalized U.S.-flag merchant marine. Some of these measures have an additional benefit; they provide an alternative or at least a method of reducing traditional direct aids—the Operating Differential Subsidy (ODS) and the Construction Differential Subsidy (CDS). The fiscal year 1982 budget provides for $417 million in operating subsidies; in the same budget, construction subsidies have been almost entirely phased out, existing largely in name only.

Neither subsidy has been an unqualified success. Operating subsidies, for example, have been unable to cover the full differential costs between U.S. and foreign-flag ships, particularly in view of the fuel cost for ships which is fifteen times greater then in 1972. Furthermore, many argue that these subsidies have encouraged inefficiency. We believe, however, that these subsidies, particularly the operating subsidy, should be continued until alternatives can be found and put in place if the U.S.-flag merchant fleet is to be more than a token presence.

CIVIL/MILITARY COOPERATION

There is one surpassing justification for a strong merchant marine—national defense. Serious deficiencies exist in America's ability to provide adequate sealift for major contingencies, particularly in view of the potential Soviet submarine threat and uncertainty of support from fleets of Allied and flag-of-convenience nations.

The Military Sealift Command is improving its sealift capabilities for smaller contingencies with programs such as the purchase of SL-7 ships, but these capabilities would be overwhelmed in a major war. Of the National Defense Reserve Fleet of 168 vessels held in storage, 130 vessels are World War II Victory Ships, and only 27 vessels in the entire reserve fleet can be made ready on a few days' notice. Furthermore, crews would have to be found and trained for most of these ships, a factor that is overlooked too often in sealift calculations or in optimistic projections about the military utility for America of foreign-flag fleets. additionally, as mentioned at the beginning, most modern commercial ships would be either unusable in many military situations or would require extensive and time-consuming alterations. We believe that the only practical solution is a strong civilian merchant marine, engaged in commerce in peacetime but designed and available for military missions when required. The Soviet merchant marine is designed in this fashion and, indeed, provides extensive support to Soviet military forces even in peacetime.

The key is close civil/military cooperation and planning at all levels; it will not be enough to institute these necessities after hostilities break out. Fortunately, cooperation and planning are already underway, but they must be ongoing and on a formal basis. The Reagan Administration, for example, plans to provide cargo support for Indian Ocean forces through civilian contract manning in the SL-7 and Maritime Prepositioning Ships Programs. Not only do these programs provide jobs that help maintain the base of trained American seamen, but they help build a pool of civilian sailors experienced in working with the Navy. In addition, some merchant ships are being provided enhancement features, such as equipment to allow direct refueling of warships by commercial tankers, that increase the ability of merchant ships to operate in a military support role if required. We recommend that these and other defense features where at all practicable be built into all new U.S.-flag ships whether constructed abroad or at home. Some of these features can be modular, standard add-ons for all ships; others must be built into ships during actual construction. The U.S. Government would have to pay for these features, or provide some other direct incentives, on vessels that are not built with Construction Differential Subsidies.

These enhancement features are an example of the kind of imaginative programs that must be undertaken if we are going to use our maritime resources to the utmost. These features cost money, but they are cheap, practicable, and versatile solutions to the potential of wartime attrition, a problem that could dangerously cripple our merchant marine and our Navy's support fleet. Because these features are far less expensive than new, dedicated Navy support ships, their use will enable the Navy to devote more funds to front-line combat capabilities.

We recommend as well two new programs to improve the military strength and utility of our merchant marine. The first is to establish an entity, funded by tax exempt shipping bonds, similar to Japan's Maritime Credit Corporation. In our case, the Corporation and the Department of Defense would finance 70–80 percent of the construction costs of a fleet of cargo ships, serially-constructed with military features and military applicability in mind, to be operated in peacetime by private shipping companies (see page 10). These would be primarily break-bulk and RO/RO ships in order to alleviate the severe shortage our sealift assets face in these types of ships. The cost of construction of the RO/RO segment could be offset by a cargo policy requiring that a percentage of foreign-manufactured automobiles be carried to the United States on U.S.-flag vessels (see page 6).

The second new program is civilian contract manning of naval support ships. If just 60 of the 71 Navy fleet support vessels were converted to civilian contract manning, more than 13,000 Navy personnel could be freed for other tasks and more than 10,000 new merchant marine jobs would be created. This would be an undertaking where every party stands to benefit. The Navy would be able to apply scarce personnel resources to more important combat tasks and at the same time build behind its fleet a supportive merchant marine, increasingly trained to operate with and supplement the Navy in time of crisis or conflict. The U.S. merchant marine would be strengthened, augmenting the number of seafaring jobs by nearly 60 percent and providing the promise of employment to attract a new generation of merchant mariners. The government would save money, because crew complements could be reduced substantially. And our nation would increase simultaneously the ability of the merchant marine to support our international objectives while enhancing our capacity for mobilization in an emergency.

IMPROVED EFFICIENCY

This paper has focused so far on actions that primarily involve the U.S. Government. Such concentration is inevitable for an industry that operates in the international arena as an extension of national economic and security policy to the degree of the maritime industry. It recognizes, as well, an inescapable fact of life: the U.S. merchant marine competes against fleets of other nations, fleets enjoying extensive governmental support and coordination. To treat the U.S. fleet as an industry that can operate unaided in today's international maritime environment will be merely to condemn this fleet to impotence and, eventually, to disappearance.

However, it would be severely misleading to imply that more effective government support is the only key to a revitalized U.S.-flag merchant marine. Labor and management, the entire maritime industry, must improve their own contributions. Increased efficiency and competitiveness—as with all American industries—must become new maritime watchwords. We are optimistic that this can result in reduced operating costs with the savings being passed on to the shipper.

Several examples of compromise are recommended. In the civilian manning of naval support ships, the labor unions should be willing to reconsider alterations in vacation practices in order to increase the financial attractiveness to the government of shifting to civilian contract manning. The advantage of labor is clear—more than ten thousand new jobs in an industry that today furnishes less than 20,000 overall. Civilian manning of naval support ships would also require a specially trained and dedicated pool of mariners, enrolled in the U.S. Navy Reserve, to guarantee availability for military needs. In this case, the merchant marine unions have already indicated their flexibility and their willingness to participate in such a pool system.

Management also must institute substantial improvements. The industry as a whole lies near the bottom of all U.S. industries in expenditures devoted to research and development. And despite the fact that many of the most innovative and revolutionary advances in ship design (i.e., container ships, RO/RO ships, LASH ships) originated in America, foreign companies in most cases have used them to best advantage. In other instances, the mistakes of management have contributed greatly to current problems facing the maritime industry. In fuel economies, U.S. vessels, which are older and use primarily steam-turbine engines, lag behind those of other nations which have successfully made the transition to fuel-efficient, slow-speed diesels. The magnitude of this factor is demonstrated by the fact that diesels can cut fuel costs by 30 percent, and fuel costs—not labor—now constitute the largest element of a ship's operating costs.

CONCLUSION

In this paper, we have recommended a series of policy initiatiaves that encompass a broad range of actions—increased cargo for U.S.-flag ships, re-flagging of foreign-flag ships to take advantage of current overtonnaging, investment stimulation to attract foreign as well as domestic sources of capital, tax policies to stimulate this investment and reduce operating costs, regulatory reform to enable U.S.-flag ship operators to compete on an equal footing with foreign companies, contined subsidies until substitutes can be put in their place, civil/military cooperation so that each sector supports the other and both strengthen the nation, and improved efficiency of management and labor alike. These initiatives, taken together, presented as part of a cohesive, Presidential policy, are the key to rebuilding the U.S.-flag merchant marine.

As we noted earlier, the U.S. merchant marine is in a time of opportunity. We believe that improvement is possible. The Reagan Administration had dedicated itself to a stronger America and with it a revitalized merchant marine; labor has shown in the past the flexibility that the future requires; and management of highly successful ship-operating companies such as Sea-Land Industries and American President Lines has conclusively demonstrated that a successful American maritime future is not pre-determined to failure but very much within our grasp.

National Marine Engineers Beneficial Association,
Washington, D.C., April 21, 1982.

Hon. **Slade Gorton,**
Chairman, Subcommittee on the Merchant Marine, Senate Commerce, Science, and Transportation Committee, Russell Senate Office Building, Washington, D.C.

Dear Senator Gorton: Our position on S. 2336, a bill to authorize appropriations for maritime programs for Fiscal Year 1982, was, I believe, adequately reflected in the letter to you from David A. Leff, Executive Director of the Joint Maritime Congress, an association of U.S.-flag ship operating companies that have collective bargaining agreements with our union. However, I am also legislative director of the AFL-CIO's Maritime Trade Department and therefore believe it is necessary to state unequivocally the position of the National Marine Engineers' Beneficial Association on the issue of the right of shipowners who receive operating differential subsidies ("ODS") to build new vessels in foreign shipyards.

Regarding attacks on the Administration and its yet-to-be-announced maritime program, we are as anxious as anyone for a White House policy decision on our debilitated fleet. However, rather than attack we have provided the Administration with a series of what we believe are workable solutions to our maritime problems. Our ideas have been well-received, and we retain our hope and patience that the White House will soon announce a program that embraces the President's campaign promises to the industry. We therefore wish to disassociate ourselves from attacks and instead we continue to pursue a constructive dialogue.

I am very much aware of the plight of the U.S. shipyards and recognize the absolute security necessity of maintaining an adequate shipyard mobilization base. Obviously, we support U.S. shipbuilding—but not at a penalty to U.S. operators. Given the current price and delivery time of U.S.-built commerical vessels, it is counterproductive to the goal of revitalizing the U.S. merchant marine to insist that ODS operators construct their vessels here unless they receive full cost parity with their foreign competitors. At present, the construction differential subsidy program limits the operator to 50 percent of vessel construction cost, a sum not adequate to give him parity with competitors who build vessels in Asia or elsewhere where the purchase price is less than half United States-built cost. The already high operating costs of the U.S. fleet are exacerbated by the higher debt service on these costlier vessels. In addition, delivery time in foreign yards is superior to that of U.S. yards, so that U.S. subsidized operators lose a competitive advantage if their technologically superior ships come on line after a competitor imitates the design plan.

U.S. shipyard supporters may argue that the same high cost accusations can be hurled at the ship operating sector. However, the single highest cost item in the operation of any vessel is fuel. U.S. ships are, in general, because of their age, the least fuel-efficient of the world's fleets and thus are the costliest to operate in terms of both fuel consumption and large crew complements. In order to lower the cost of operating U.S.-flag ships, it is necessary to build cheaper, modern and more cost- and service-competitive vessels. This will not happen unless ODS operators are permitted to build in foreign yards or receive full cost parity here (which is unlikely, given federal budget considerations).

For the foregoing reasons, your amendment is a good one that recognizes the need for foreign building on a long-term basis to enable operators to make long-range plans, and we support it in the interest of building a larger, more modern and more cost-effective U.S. merchant marine.

Respectfully,

Jesse M. Calhoon,
President.

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